THE
INCOME TAX REPORTS

A JOURNAL OF
THE LAW OF INCOME TAX AND EXCESS PROFITS TAX
WITH
REPORTS OF
INDIAN AND SELECT ENGLISH CASES

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NOTES AND COMMENTS

MANAGING AGENCY AGREEMENTS AND EXCESS PROFITS TAX.

The recent decision of the House of Lords in *L. C., Ltd.* v. *G. B. Ollivant, Ltd., and others* [1] reported in the 1st December issue of the INCOME-TAX REPORTS relates to a subject which is of great importance to commercial circles in general and managing agents in particular.

A FUNDAMENTAL PRINCIPLE OF TAXATION

It is a fundamental principle of the law of taxation which, as Lord Simon has said, "*has been explained once and for all in the well-known case of Ashton Gas Co.* v. *Attorney-General* [2]" that the profits of a trading company according to ordinary commercial practice are the profits before and not after deducting the direct taxation which has to be paid in respect of them. This principle has been consistently applied with regard to income-tax; and it has been universally recognized since the date of that decision that income-tax is not a deduction which has to be made in order to arrive at profits.

NATURE OF EXCESS PROFITS TAX

What about excess profits tax? It is also undoubtedly a tax on profits and there is nothing from a purely legal point of view to differentiate excess profits tax from income-tax for the purposes of the application of this principle. Both in its purport and essence it is a tax on profits. The big proportion that excess profits tax bears to profits has, however, clouded its true legal nature and created some confusion in England, and in India also, in the application of the rule in *Ashton Gas Co.'s case* [2] to excess profits tax. There were conflicting decisions in England on the question, and attempts have been made in some cases to avoid the inequality of shares and hardship that may result in particular circumstances by the application of this doctrine, by narrowing the ordinary legal and commercial conception of the word profits by limiting it to divisible or distributable profits and thus excluding excess profits tax from "profits."

THE OLLIVANT CASE

The latest decision in England on the point is that of the House of Lords in *L.C., Ltd.* v. *G. B. Ollivant, Ltd., and others* [1] in which Lord Simon (the Lord Chancellor) and Lord Macmillan have taken the view that excess profits tax should not be deducted in the computation of "profits"; and Lord Thankerton, Lord Russell of Killowen and Lord Wright have taken the opposite view. With regard to this case the reports show that Lord Simon and Lord Macmillan have considered

(1) (1945) 13 I.T.R. Suppl. 23. (2) [1906] A.C. 10.

in detail the principles on which the matter should be decided and, as observed in the Editorial Note[1] in the *All England Reports*, "Lord Wright is the only member of the majority who has dealt with the reasons why excess profits tax must be dealt with in a way different from that which has always been applied to income-tax." The opinion of the Lord Chancellor (Lord Simon) on questions of law in general, and that of Lord Macmillan on questions of revenue law, are entitled to exceptionally great weight, and, after a careful study of all the judgments delivered before the House of Lords, we are not convinced that there is any principle of law upon which excess profits tax can be distinguished from income-tax for the present purpose. No doubt, excess profits tax is very heavy and the respective shares may sometimes be affected very much to the prejudice of one of the parties if the doctrine which is applicable to taxes on income in general is applied to this kind of tax, but this circumstance should certainly not be allowed to mislead us from the true legal aspect of the question and induce us to come to conclusions which are not warranted by law.

POLICY OF THE INDIAN LEGISLATURE

In India the true principle has been recognised and the view that should be adopted has been embodied in the Companies Act by the Indian legislature when that Act was overhauled in 1936. Section 87-C provides that where the remuneration of a managing agent is based on a fixed percentage of the net annual profits of the company, "net profits" shall be taken to mean the "profits without any deduction in respect of income-tax or super-tax or any other tax or duty on income or revenue." This section, we would strongly emphasize, merely incorporates in the statute the general principle laid down in *Ashton Gas Co.'s case*. It also lays down clearly the policy that should be adopted in India. It makes no distinction between income-tax and excess profits tax and rightly places all taxes on income on the same footing. Section 87-C does not change the law but merely enacts the general principle to remove all doubts about the applicability of the rule to India. To agreements which came into existence before the date of the commencement of the Amendment Act of 1936 the same rule would apply on general principles. The definition of "taxes on income" contained in the Government of India Act, Section 311, is also relevant so far as India is concerned. Excess profits tax is expressly included in the expression "taxes on income."

INDIAN DECISIONS

The law as above stated was correctly understood and applied in *Finlay's case*[2]. In this case a managing agency agreement provided that in ascertaining profits on which the commission was based no deduction was to be made for "income-tax, super-tax or any other tax

(1) (1944) 1 A.E.R. 510, at p. 511. (2) (1942) 47 Bom. L.R. 774.

on income," and excess profits tax was rightly held to be a tax on income and not deductible in computing the net profits. In a later case which came up before the Bombay High Court, *Walchand and Co.'s case* [1], there was no express provision with reference to deduction of taxes as in *Finlay's case*, and the High Court held that though income-tax should not be deducted, excess profits tax must be deducted. The Judges have not overruled or dissented from *Finlay's case*. One could understand the judgment even though he may not agree with it, if they had said that neither income-tax nor excess profits tax could be deducted. This decision cannot be reconciled with *Finlay's case* and most of the arguments advanced by Beaumont, C. J., in support of his conclusion are unconvincing.

In this connection it is worthy of note that in a still later case, *The Premier Construction Co.* v. *Commissioner of Income-tax, Bombay* [2], Chagla, J., has cast doubts on the judgment in *Walchand and Co.'s case*. Chagla, J., said : " Now in the course of his judgment Beaumont, C. J., did use the expression that that agreement was a profit sharing agreement. *But the question is in what profits did the managing agents share? It is clear that the profits in which the managing agents shared were not the same profits in which ultimately the shareholders had a right to share or the profits which ultimately became divisible amongst the shareholders.* With respect to the learned Chief Justice a confusion is created by using the expression profits which has different connotations in different contexts."

Again, *Ashton Gas Co.'s case* lays down a well-known principle as to computation of profits. Agreements relating to profits are drafted by lawyers and signed by the contracting parties on the assumption that they would be construed and interpreted in the light of that principle—in other words, as if the principle of *Ashton Gas Co.'s case* were one of the terms of the agreement.

MANAGING AGENCY AGREEMENTS

Directing our attention to managing agency agreements in particular it is clear that the decision in the *Ollivant case* is not directly applicable. Where the question is one of measuring capital in terms of profits, as in the *Ollivant case* and the old case of *Collins* v. *Sedgwick* [3], or the question is one of distributing profits to shareholders or to partners, it may perhaps be appropriate, in the absence of any other indication in the contract to the contrary, to refer the " profits" to the *divisible* amount, *after* all outgoing items, including taxes, have been met. But what is paid to an employee or a managing agent, is not a share of divisible profits in this sense, unless the contract so expressly defines it. It is rather of the nature of a prior charge on the ultimate profits, like any other item of necessary expenditure for earning

(1) (1944) 12 I.T.R. 104. (2) (1945) 13 I.T.R. 391. (3) (1917) 1 Ch. 179.

the profits; and if the item is referred to as a share of "profits," the word "profits" in that connection is used not in the *ultimate*, but in an *intermediate* sense. Even in the case of an employee, if the contract makes it clear, the remuneration may well be partly a *prior* charge and partly a share of the *ultimate* profits. The interpretation put by the majority in the *Ollivant case* that "profits" mean "distributable profits" is on the face of it inapplicable to managing agency agreements, as the share of the profits payable to the managing agent is not a part of the distributable profits at all.

PRACTICAL DIFFICULTIES

There are some other serious and, in our opinion, unanswerable objections to the view adopted in *Walchand and Co.'s case*.

First, excess profits tax of a given year is only a *provisional* payment which may be refunded in later years, by adjustment of deficiencies. Can there be any justification from a legal or commercial point of view for putting a construction upon an agreement which would disentitle the employee to the benefits which may accrue through refunds while making him bear the burden of sharing in the provisional advance payments alone?

Again, it very often happens, when there are several businesses or branches that the agent may be remunerated by a share of profits of one or a small block of the businesses, and the injustice of making the share of the agent depend on the fate of businesses or branches with which he has no concern whatever is obvious.

The assumption made by Beaumont, C. J., in *Walchand and Co.'s case* that if excess profits tax is not deducted first, the Exchequer may suffer—a fact which is, by the way, wholly irrelevant on a question like this—is also unfounded. On the contrary, the Exchequer would, more often than not, benefit.

CONCLUSION

From a jurist's point of view we are decidedly of opinion that the Lord Chancellor and Lord Macmillan have come to the right conclusion in the *Ollivant case* and that there is nothing in law to justify a departure from the rule laid down in *Ashton Gas Co.'s case* in the matter of excess profits tax. Even otherwise, we think that in the face of Section 87-C of the Indian Companies Act, by which the Indian Legislature has deliberately laid down the policy that should be adopted in India, it is not proper to extend to India a view which has been so strongly opposed in England by the Lord Chancellor and Lord Macmillan and over which the public even in England have not been feeling very happy. In any event agency agreements should be looked at from an entirely different standpoint from proprietary agreements like those in the *Ollivant case*.

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NOTIFICATIONS.

Income-tax Establishments.

Notification No. 7-Camp. dated the 15th December, 1945.

In pursuance of sub-section (4) of Section 5 of the Indian Income-tax Act, 1922 (XI of 1922), the Central Board of Revenue directs that the following further amendments shall be made in its Notification No. 58 Income-tax, dated the 15th July 1939, namely :—

In the Schedule appended to the said Notification under the sub-head "II-Bombay, Sind, British Baluchistan and Ajmer-Merwara" for the Income-tax Circles specified against the Bombay 'B' and Bombay 'D' Ranges, the following Income-tax Circles shall be substituted respectively, namely :— .

"*Bombay 'B' Range.*—

(1) Companies Circle I (all sections).
(2) Companies Circle II (all sections).
(3) Companies Circle III (all sections).
(4) Companies Circle IV (all sections).
(5) C-I Ward.
(6) C-IV Ward.
(7) Air Force Circle, Bombay.

Bombay 'D' Range.—

(1) Bombay Circle I.
(2) Bombay Circle II.
(3) Bombay Circle III.
(4) Bombay Circle IV.
(5) Bombay Circle V.
(6) Bombay Circle VI.
(7) Bombay Circle VII.
(8) Bombay Circle VIII.
(9) Bombay Circle IX.

Bombay 'D' Range.—(Contd.)

(10) Bombay Circle X.
(11) Bombay Circle XI.
(12) Bombay Circle XII.
(13) Central Section I.
(14) Central Section II.
(15) Central Section III.
(16) Central Section IV.
(17) Central Section V.
(18) Central Section VI.
(19) Central Section VII.
(20) Central Section VIII.
(21) Central Section IX.
(22) Central Section X.
(23) Central Section XI.
(24) Central Section XII.
(25) Salaries Section I.
(26) Salaries Section II.
(27) Bombay Refund Circle."

Notification No. 10-Camp. dated the 29th December, 1945.

In pursuance of sub-section (4) of Section 5 of the Indian Income-tax Act, 1922 (XI of 1922), the Central Board of Revenue directs that with effect from the 1st December 1944, the following further amendment shall be made in its notification No. 58-Income-tax, dated the 15th July 1939, namely :—

In the Schedule appended to the said notification, under the sub-head "IV-United Provinces and Central Provinces and Berar," after entry No. (12) against Nagpur Range, the following entry shall be added, namely—

"(13) Income-tax *cum* Excess Profits Tax Circle, Nagpur."

Notification No. 11 Camp dated the 12th January, 1946.

In pursuance of sub-section (4) of Section 5 of the Indian Income-tax Act, 1922 (XI of 1922), the Central Board of Revenue, directs that with effect from the 21st January 1946, the following further amendment shall be made in the schedule appended to its notification No. 58-Income-tax, dated the 15th July 1939, namely :—

In the said Schedule under the sub-head "IV-United Provinces and Central Provinces and Berar" for the Ranges Lucknow, Agra and

Cawnpore and the Income-tax Circles specified against them, the following Ranges and Income-tax Circles shall be substituted, namely :—

Cawnpore—
(1) Cawnpore
(2) Special Income-tax *Cum* Excess Profits Tax Circle, Cawnpore.

Agra—
(1) Agra.
(2) Fatehgarh.
(3) Aligarh.
(4) Meerut.
(5) Military Circle, Meerut.
(6) Saharanpur.
(7) Dehra Dun.

Lucknow—
(1) Lucknow.
(2) Fyzabad.
(3) Gonda.
(4) Sitapur.
(5) Bareilly.
(6) Moradabad.
(7) Jhansi.

Benares—
(1) Benares.
(2) Allahabad.
(3) Central Circle, Allahabad.
(4) Azamgarh.
(5) Gorakhpur.

Income-tax (Double Taxation Relief) (Indian States) Rules, 1939—Amendments.

Notification No. 9-Camp. dated the 29th December, 1945.

In exercise of the powers conferred by Section 49A of the Indian Income-tax Act, 1922 (XI of 1922), the Central Government is pleased to direct that the following further amendments shall be made in the Income-tax (Double Taxation Relief) (Indian States) Rules, 1939, namely :—

1. (1) Add the following clauses to rule 2—

"(e) the expression "corresponding year" in relation to a year of assessment in British India means the year for the purposes of State income-tax which by order of the Central Board of Revenue shall be deemed to correspond with such year of assessment in British India.

(f) the reference to the lower of the two rates shall where the rates are equal, be construed as a reference to either of those two rates."

(2) For rule 3 substitute the following rule.

"If any person who has paid by deduction under Section 18 of the Indian Income-tax Act, 1922, or otherwise, Indian Income-tax for any year on any part of his income proves to the satisfaction of the Income-tax Officer that he has paid for the corresponding year by deduction or otherwise State income-tax in respect of that part of his income, he shall be entitled to the refund of Indian Income-tax calculated on that part of his income at a rate bearing to the Indian rate of tax or the State rate of tax, whichever is the lower, the same proportion as the Indian rate of tax bears to the sum of the Indian rate of tax and the State rate of tax: *Provided* that where in respect of that part of the income relief has already been obtained under this rule on account of taxation in another State or further relief is admissible in British India on account of taxation in the United Kingdom or Ceylon, the refund shall be so regulated that together with such other relief the aggregate relief shall not exceed half the Indian rate of tax."

2. The amended Rules shall apply to assessments made in British India for and from the year beginning on the 1st April 1942.

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Auditor's Certificates Rules, 1932—Amendments.

Notification No. 1-A (7)/45 dated the 22nd December, 1945.

In exercise of the powers conferred by sub-section (2) of Section 144 of the Indian Companies Act, 1913 (VII of 1913), the Central Government is pleased to direct that the following further amendments shall be made in the Auditor's Certificates Rules, 1932, the same having been previously published as required by the said sub-section, namely :—

In the said Rules—

(1) for the word "three" in sub-rule (a) of rule 40 (1), the word "four" shall be substituted ;

(2) for the word "four" in the proviso to sub-rule (a) of rule 40 (1), the word "five" shall be substituted ;

(3) for the word "four" in sub-rule (b) of rule 40 (1), the word "five" shall be substituted.

Notification No. 1-A(5)/45 dated the 29th December, 1945.

In exercise of the powers conferred by sub-section (2) of Section 144 of the Indian Companies Act, 1913 (VII of 1913), the Central Government is pleased to direct that the following further amendments, which are proposed to come into force on the respective dates given in the footnotes, shall be made in the Auditor's Certificates Rules, 1932, the same having been previously published as required by the said sub-section, namely :—

In the said Rules :—

(1) for rule 22 the following rule shall be substituted, namely :—

" * 22. No candidate shall be admitted to the First Examination unless he—

(1) is a graduate, or

(2) is eligible for admission under rule 24, or

(3) has (a) either—

(i) entered into service under articles before the 1st January 1946, or

(ii) rendered military service in connection with a war in which His Majesty's Government is involved and passed the Matriculation Examination of a University constituted by law in British India or British Burma or the University of Mysore or the Osmania University, or an examination entitling him to enter upon a course of studies of any such University, or an examination which has been declared by the Central Government to be equivalent thereto, or

(iii) passed the Intermediate Examination of any of the aforementioned Universities or an examination recognised by the Central Government as equivalent thereto ;

and (b) produces either—

(i) a certificate in the form given in Appendix 4 from the head of an institution recognised for the purpose by the Central Government that he has, subsequently to passing such examination, studied

for a period of one academic year at such an institution and is fit to present himself for the examination, or

(ii) a certificate that he has served for not less than seven years either wholly as an audit clerk or partly (but for not less than three years) as such clerk and partly as an articled clerk (in the latter case one complete year's service as an articled clerk being reckoned as two years' service as audit clerk and fractions of a year being ignored), or

(iii) evidence to show that he was at any time admitted to the Examination for the Government Diploma in Accountancy held by the Accountancy Diploma Board, Bombay, or was eligible for admission to that Examination:

Provided that—

(1) a candidate who produces a certificate in the form given in Appendix 4 in respect of a period of study prior to 1946-47 shall be eligible for admission on passing the Intermediate or equivalent examination; and

(2) a candidate who has passed the Matriculation or equivalent examination shall be eligible for admission to the First Examination to be held in 1947 if he either—

(i) has entered into service as an audit clerk before the 1st October 1945 and produces the certificate referred to in sub-clause (i) of clause (b) of this sub-rule, or

(ii) fulfils the requirements of sub-clause (ii) of clause (b) of this sub-rule, or

(iii) has appeared and failed at any of the First Examinations held before 1947.

NOTE:—*This rule shall come into force from the 1st May 1946."

(2) in rule 22-A, between the words "clause (b)" and the words "of rule 22" the following words, figure and brackets shall be inserted, namely:—

"of sub-rule (3)."

NOTE:—This amendment shall come into force from the 1st May 1946.

(3) for rule 41 the following rule shall be substituted, namely:—

"*41. A Registered Accountant entitled to train articled clerks shall before accepting a person for service under articles with him satisfy himself by inspection of the relevant certificates that such person—

(a) will be not less than sixteen years of age on the date of commencement of his articles, and

(b) has passed the Intermediate Examination of a University constituted by law in British India or British Burma or of the University of Mysore or of the Osmania University or an examination recognised by the Central Government as equivalent thereto. Provided that a person shall be accepted for service under articles if he—

(1) has passed the Matriculation Examination of any of the said Universities or an examination which has been declared by the Central Government to be equivalent thereto and has rendered military service in connection with a war in which His Majesty's Government is involved, or

(2) has passed the examination prescribed for the Government Diploma in Accountancy or an examination recognised as equivalent thereto by the Regulations for the award of the Government Diploma in Accountancy or the First Examination, or

(3) had before the 1st October 1945 entered into service under articles with a Registered Accountant entitled to train articled clerks.

NOTE :—* This rule shall come into force from the 1st January 1946."

Notification No. 1-A (8)/45 dated the 2nd February, 1946.

In exercise of the powers conferred by sub-section (2) of Section 144 of the Indian Companies Act, 1913 (VII of 1913), the Central Government is pleased to direct that the following further amendment shall be made in the Auditor's Certificates Rules, 1932, the same having been previously published as required by the said sub-section, namely :—

To rule 27 of the said Rules, the following proviso shall be added, namely :—

" provided that if the Central Government is satisfied that a candidate has not availed himself of the concession of appearing only for the remaining group by reason of his absence on military duties in connection with a war in which His Majesty's Government is involved or by reason of occupation of Burma or the Far East by the Enemy, he shall be allowed to take the chances within two years of his release from war service or within two years of re-occupation of Burma or the Far East as the case may be."

Notification No. 1-A (8)/44 dated the 16th February 1946.

In exercise of the powers conferred by sub-section (2) of Section 144 of the Indian Companies Act, 1913 (VII of 1913) the Central Government is pleased to direct that the following further amendments shall be made in the Auditor's Certificates Rules, 1932, the same having been previously published as required by the said sub-section, namely:

In Appendix 3 to the said Rules :—

(1) In item (5), for the words " like means" the words, "means partaking of the nature of advertisement " shall be substituted.

(2) After item (5), the following Note shall be inserted, namely :—

" NOTE :—The use of any designation or expression except " Registered Accountant " on professional documents, visiting cards or sign boards shall be construed as " advertisement " within the meaning of the above item unless it be—

(*a*) A title of honour conferred by Government;

(*b*) A title indicating membership of a recognised Institute or Society as specified in Rule 7 of the Auditor's Certificates Rules, 1932 ;

(*c*) A degree of a University constituted by law in the United Kingdom or Burma or India without reference to any special merit or distinction achieved ;

(*d*) The letters " G.D.A." and/or the designation " Government Diplomate in Accountancy " ; or

(*e*) The word " Auditor " or " Auditors."

2. Registered Accountants entitled to style themselves as " Certified Accountants " according to the Auditor's Certificates Rules of

an Indian State, who are not members of the Scottish Institute or Society of Chartered Accountants shall not use the letters "C.A." after their names without specifying the source from which the designation has been acquired."

Restricted Certificates Rules, 1932—Amendments.

Notification No. 1-A (8)/44 (I) dated the 16th February 1946.

In exercise of the powers conferred by sub-section (2) of Section 3 of the Indian Companies (Amendment) Act, 1930 (XIX of 1930), the Central Government is pleased to direct that the following further amendments shall be made in the Restricted Certificates Rules, 1932, the same having been previously published as required by the said sub-section, namely :—

In the Appendix to the said Rules—

(1) In item (5), for the words "like means" the words, "means partaking of the nature of advertisement" shall be substituted.

(2) After item (5), the following Note shall be inserted, namely :—

"NOTE :—The use of any designation or expression except "Restricted Certified Accountant" on professional documents, visiting cards or sign boards shall be construed as "advertisement" within the meaning of the above item unless it be—

(*a*) A title of honour conferred by Government ;

(*b*) A title indicating membership of a recognized Institute or Society as specified in Rule 7 of the Auditor's Certificates Rules, 1932 ;

(*c*) A degree of a University constituted by law in the United Kingdom or Burma or India without reference to any special merit or distinction achieved ;

(*d*) The letters "G.D.A." and/or the designation "Government Diplomate in Accountancy" ; or

(*e*) The word "Auditor" or "Auditors."

2. Restricted Certified Accountants entitled to style themselves as "Certified Accountants" according to the Auditor's Certificates Rules of an Indian State shall not use the letters "C.A." after their names without specifying the source from which the designation has been acquired."

Indian Income-tax Rules, 1922—Amendments.

Notification No. 12-Camp dated the 2nd February 1946.

In exercise of the powers conferred by sub-section (1) of Section 59 of the Indian Income-tax Act, 1922 (XI of 1922), the Central Board of Revenue directs that the following further amendment shall be made in the Indian Income-tax Rules, 1922, the same having been previously published as required by sub-section (4) of the said section, namely :—

In item 7 of the statement set forth in rule 11A of the said Rules, for the words "at or in connection with the termination of employment" the words "from an unrecognised provident fund" shall be substituted.

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EXTRACTS FROM BUDGET SPEECH 1946-47

Financial year, 1945-46.

Total revenue receipts are now expected to reach Rs. 360·66 crores, a decrease of Rs. 1·68 crores on the budget estimates.

Under taxes on income, we estimated a collection of Rs. 190·5 crores, Rs. 90 crores under excess profits tax and Rs. 100·5 crores under other taxes on income. We now place the revenue at Rs. 189 crores, the short-fall of Rs. 1½ crores occurring under ordinary income-tax. The divisible pool of income-tax is likely to amount to Rs. 55·94 crores and the share of the Provinces together with the carry over of Rs. 5·28 crores from the previous year, to Rs. 28·75 crores.

Financial year, 1946-47.

I turn now to the financial year 1946-47. Before taking into account fresh taxation proposals and an adjustment to which I shall refer later, our total revenue estimates amount to Rs. 307 crores compared with Rs. 362·34 for the current year.

Now that war activities have ceased, we are allowing for a total revenue of Rs. 158 crores only under corporation and income-taxes. This includes an expected yield of Rs. 75 crores from excess profits tax. The divisible pool of income-tax has been taken at Rs. 46·79 crores and the share available to Provinces at Rs. 19·64 crores.

Taxation Enquiry Committee.

Before I explain the taxation proposals for next year, there is one further matter to which I would like to refer. A widespread desire has been expressed for the appointment of a committee to examine and report on the present tax structure and taxation incidence, with special reference to their effect on trade, industry, employment, standard of living, savings and capital formation. The Government appreciate that more than 20 years have elapsed since the last general enquiry into taxation in India was held, and that the situation has in many ways changed materially since then, particularly during the six years of war. Not least of the changes has been the re-orientation of economic thought in the interval. With the cessation of hostilities and an era of intensive development begun, which will require constructive planning of taxation with a view to ensuring the most effective use of the taxable resources of the country, the present may reasonably be regarded as ripe for a fresh comprehensive taxation review. I propose, therefore, to set up a Taxation Enquiry Committee in the near future. Since one important object of the proposed enquiry would be to secure, as between the various classes of taxpayers, an equitable distribution of the burdens of taxation, it would seem to be essential that, as in the case of the Taxation Enquiry Committee of 1924, the scope of the enquiry should extend to the whole field of taxation—Central, Provincial and local. While it would not be appropriate for the Committee to

concern itself with the question of the distribution of taxable resources between the Centre and Provinces, it should cover the harmonisation of Central and Provincial taxation where experience has shown conflict or overlap to exist in their respective spheres, as defined in the Constitution Act. The present lack of uniformity in the incidence of taxation as between Provinces, illustrated by the varying rates of sales tax, octroi, property tax, motor taxation, etc., could be dealt with by the Committee. The main purpose of the enquiry would, however, be to ascertain what adjustments or modifications of the taxation system of the country as a whole would be required and could, from the practical administrative point of view, be introduced in order to produce a properly balanced and scientific tax structure, fair in its incidence and adequate to the needs of a forward development policy, without deterrent effect on initiative and private enterprise, and with due regard to the administrative requirements for the prevention of tax evasion. The Provinces are in favour of an enquiry of this nature. My provisional view is that the Committee should be predominantly non-official in character and that it should be an expert rather than a representative body, although care should be taken to obtain the views of all the interests affected,—industry, commerce, agriculture, labour, the consumer, the ordinary taxpayer and lastly, the Administration, both Central and Provincial. Above all, it should not be unwieldy. There appears to me to be in India a tendency to set up not only too many committees but also committees which are quite unmanageable from the point of view of size. I shall greatly welcome the views of Hon'ble Members as to the scope and composition of the Committee.

I now pass to my taxation proposals for next year.

New proposals.

I said early that fiscal policy was not an end in itself. It must subserve the ends of national policy. Its purpose should be not merely to raise a given revenue but to raise it in such a way as to obtain the maximum social and economic advantage and to distribute the burden as justly and as fairly as possible between the various classes of taxpayers. This is, of course, an ideal which it is difficult to achieve in this imperfect world, where psychological and political factors operate to modify and qualify economic theory and doctrine, but the pattern and design of my proposals attempt to conform as near as possible to this ideal.

The lines of this pattern are made plain in the opening paragraphs of my speech. Let me recall briefly the gist of those paragraphs. I pointed out, first that a great deal of money would be required to combat the evils of poverty, ill-health, squalor, illiteracy and unemployment; and secondly, that during the next year or two Government must do all it can to offset the fall in economic activity which will otherwise result from the heavy drop in military expenditure.

The largest single source of revenue in the years immediately ahead will have to continue to be the profits of industry. I am conscious of the depressing effect on industrial enterprise of a high level of taxation on profits, and that it is the expansion of industry which holds out the earliest promise of increasing the national income and raising the standard of living in the country, although India will not achieve

the maximum of economic health and wealth until agriculture as well as industry have multiplied their productivity many times.

The fiscal problem, so far as industry is concerned, is how to lay it under a heavy contribution and, at the same time, to encourage it to expand. This is the problem which I have attempted to solve, but its successful solution will require the whole-hearted co-operation of industry itself. If it be the aim of India's industrial leaders, as I am sure it is, not so much to make millions for themselves as to raise the standard of life of India's toiling and poverty-stricken millions, then the problem can be solved.

Excess Profits Tax.

Here is my own contribution to its solution. First, I propose to discontinue the Excess Profits Tax on earnings arising after the 31st March, 1946. The only justification for E. P. T. as a tax is the emergency which called it into being. By all the canons of taxation doctrine it is a thoroughly bad tax. It is rough and ready in its operation; it is unfair in its incidence and, beyond a certain point, it is a direct inducement to inefficiency. Except that I, as tax gatherer-in-chief, cannot refrain from casting a longing, lingering look behind at its high yield, none of us will, I think, mourn the passing of the Excess Profits Tax.

It will, of course, be realised that the discontinuance of the tax will not, of itself, affect the revenue of the coming year nor give any immediate relief to the class of taxpayer to whom it applies, since the tax will still be payable in respect of all excess profits earned up to the 31st March, 1946. The scheme of compulsory deposits will also remain in force to the end of the E. P. T. period.

As regards the refunds of E. P. T. deposits, they will be sanctioned in advance of the date for which the law provides, on condition that they are not distributed as dividends to shareholders but are required for the provision or replacement of buildings, plant or machinery.

When I remind the House that E. P. T. will yield Rs. 90 crores in the current year and is estimated to produce Rs. 75 crores in the coming year, Honourable Members will be able to measure the loss to revenue and the benefit to industry which the abandonment of E. P. T. implies.

One last word about E. P. T. Concern has been expressed about losses and expenditure which may arise in the period of transition from war-time to peace-time conditions and which may involve hardship if they are not allowed against the profits of the final E. P. T. chargeable accounting period. This question is under consideration and, when it is known what is the actual extent and nature of these hardships, then will be the time to consider appropriate legislation.

Special initial depreciation.

The next relief to industry which I propose is to revive the proposals which were dropped last year to grant special initial depreciation allowances of 10 per cent. on new buildings and of 20 per cent. on new plant and machinery and to allow for income-tax purposes expenditure on scientific research. In addition, I propose to widen the scope of what is called the obsolescence allowance, so as to make it include the

loss of the asset by destruction or demolition and also to extend it to buildings. These proposals will cost Rs. 2 crores.

In order to complete the picture of the easements which I propose for industry, I shall now move to the field of indirect taxation. I shall return later to other direct taxation proposals which will affect industry.

Customs duty of raw materials.

I am anxious at the earliest possible moment to meet the demand so often made in the past for the relief from Customs duty of raw materials imported for industry; and also, to the extent that this may be practicable without injury to Indian manufacturers of similar goods, to reduce the rates on such imported plant and machinery as are now dutiable. The former proposal is estimated to cost approximately Rs. 70 lakhs. As regards the latter, it is difficult to estimate the cost of relief till a careful review of the position is made. So no allowance has been made in the revenue estimates on this account at this stage. It is proposed to give effect to the decisions separately by a notification under the Sea Customs Act.

Amalgamation of surcharge with basic rates.

I now revert to the direct taxation field but, before dealing with it as it specially affects industry, I should like to mention a proposal which will affect not only all classes of taxpayers but also Central and Provincial Revenues, namely, the amalgamation of the surcharges on income-tax and super-tax with the basic rates. This amalgamation is estimated to benefit the Provinces to the extent of Rs. 12¾ crores at the expense of the Centre.

Tax on companies.

Coming back to industry, the total of the present rates of income-tax and super-tax on a company is 7¾ annas. I propose to reduce this total of 7¾ annas by 1¾ annas to 6 annas, by a reduction of 2 annas in the super-tax and an addition of ¼ anna to the income-tax. This is estimated to cost Rs. 7 crores. For the past two years the Finance Act has contained a provision giving a rebate of super-tax to companies at the rate of one anna on all sums not distributed as dividends. This, in effect, imposed an extra tax at the rate of one anna on all sums distributed as dividends. I think that circumstances now warrant the introduction of a new method for discouraging the distribution of dividends. In my view, a reasonable distribution is something which the shareholder has a right to expect and which should not attract a penal rate of tax. I am, therefore, proposing that, excluding dividends payable at a fixed rate, sums equal to 5 per cent. on the capital of the company, including reserves, and equal to 30 per cent. of the total income, may be distributed without attracting more than the 1 anna rate of super-tax. Dividends above that datum line will become liable to additional super-tax at steepening rates. I hope that this provision will keep the distribution of dividends within reasonable bounds and encourage the ploughing back of profits into the business. This is estimated to yield about Rs. 1½ crores.

Income-tax relief for new buildings.

Before turning to the non-company direct taxpayer, it will be appropriate to mention at this stage another and somewhat novel proposal which affects both classes. I have referred more than once to the possible emergence of deflationary tendencies consequent upon the very heavy fall in military expenditure, and I reminded the House that, owing to the difficulty experienced by our industries in obtaining adequate quantities of capital equipment from abroad, they would not be able to do a great deal next year to replace the economic activity engendered by the vast military expenditure of recent years. There is, however, one direction in which the private sector of the national economy can do much to help. I mean, of course, building, which has been almost at a standstill, except for war purposes, for the past five or six years. The great advantage of a large building programme is that the ratio of labour costs to total costs is high and so, therefore, is the employment factor. Apart from the offer of subsidies for working-class dwellings which I have already mentioned, Government are doing all they can to assist by increasing the free availability (but by this expression I do not, of course, mean free of cost) of bricks, timber, cement and steel. But so important do I regard private building as an antideflationary activity that I have felt justified in going further and in making a contribution in the fiscal field. I am, therefore, proposing some income-tax relief where new buildings are begun and completed within the next two years. For residential buildings, I propose a two years' income-tax exemption and for buildings used for the purposes of the business, profession or vocation I propose that the initial depreciation allowance should be 15 per cent. instead of 10 per cent. These proposals are contained in a Bill to amend the Income-tax Act which is being put before the House. As next year's estimates are not likely to be affected, no provision has been made on this account.

Income-tax on lower incomes and earned income relief.

And now I turn to greet the ordinary direct taxpayer, and I hope that, on reading tomorrow morning what I have to say, he will think the greeting cordial, or at any rate, as cordial as any greeting between an Income-tax Officer and an assessee can reasonably be expected to be. In my judgment, the steep rise in direct taxation inseparable from the war has borne more heavily on the man of moderate means and particularly on the man with a moderate fixed income than on almost any other class of taxpayer. I think the time has come to give him some relief. I propose to do this in two ways. First, by reducing the rate of tax in the lower ranges and secondly by increasing the earned income allowance. As to the first, I propose to reduce the rate on the second income slab of Rs. 3,500 from 15 pies to 12 pies, and the rate on the third slab of Rs. 5,000 from 2 annas 1 pie to 2 annas. These two changes will cost about Rs. 1½ crores. As to the second, I propose to raise the earned income allowance from one-tenth of the earned income, subject to a maximum of Rs. 2,000 (in terms of income), to one-fifth, subject to a maximum (in terms of income), of Rs. 4,000. This relief will cost about Rs. 3½ crores.

I propose to take a further and, as I think, a logical step in carrying over the differentiation of treatment between earned and unearned income into the super-tax range. At the same time, I propose to increase the number of slabs in incomes subject to super-tax, the result being a more gradual steepening of the rates, although the rates will be more severe on the largest incomes than at present. The differentiation in favour of earned income is one anna in the rupee between Rs. 25,000 and up to Rs. 2 lakhs and half an anna between Rs. 2 lakhs and Rs. 5 lakhs. On the balance above Rs. 5 lakhs there is no differentiation. This proposal is estimated to yield about Rs. 75 lakhs. On merits, and as a partial offset to the loss of revenue involved in the three changes which I have just described, I propose to increase the rate of income-tax on the balance of income above Rs. 15,000 from 4 annas 9 pies to 5 annas. This will yield about Rs. 3¼ crores.

Other minor changes.

With two other and relatively minor changes I shall be done with my proposals relating to direct taxation. The first is a reduction of the rate on life insurance companies from 5 annas 3 pies to 5 annas. The second relates to the discontinuance of the provision for funding a portion of the tax in the case of incomes up to Rs. 6,000. The reductions in the rates on the lower slabs and the increased earned income allowance now proposed take away the justification for this provision. Salaried assessees, however, have to be given the benefit of the provision in the coming year, since they came under the scheme one year later than other assessees. These two proposals are estimated to cost Rs. 25 lakhs.

Relief for the poor.

I have now dealt with relief to industry and to the man of moderate means, and some of my Hon'ble Friends opposite will be wondering whether I propose to do anything for the poor man. In the field of direct taxation, I can obviously do nothing since he does not pay direct taxes. At least he does not pay them directly. The extent to which an increase or a decrease in direct taxation is passed on to him through the price of the articles he has to buy is one of the things which I hope that the proposed Taxation Enquiry Committee will examine and ascertain.

Nor is it easy to do very much for the poor man in the field of indirect taxation. The main advantage which he will derive from my proposals will be through the schemes, economic and social, which will be financed by the yield of the taxes contributed by the wealthier sections of the community.

Duty on kerosene.

But there are two other things which I am doing for the poor man, one negative and the other positive. As to the first, I do not think that any of my proposals will add to the cost of his essential purchases —indeed the contrary should be the case—and secondly, I propose to reduce the duty on kerosene, which plays so important a part in the economy of the poorer class households, from 4 annas 6 pies to 3 annas

9 pies an imperial gallon. This will cost about Rs. 65 lakhs, of which Customs will bear Rs. 60 lakhs.

Other indirect taxation proposals.

And this brings me to my other indirect taxation proposals. I propose to continue (subject to some modifications) the general surcharge for one more year. In the customs tariff a small change is proposed in respect of "wines." The rate of surcharge on "wines," which is now one-fifth, will be raised to one-half, thereby bringing it on a par with "spirits." I expect an increase of revenue by about Rs. 5 lakhs on this account. The duty on cinematograph films, both exposed and not exposed, is at present assessed on *ad valorem* rates. It will be an improvement to convert this into a specific duty charged on footage, and this change, besides yielding an increased revenue of Rs. 45 lakhs, will make for administrative convenience.

In the interests both of the revenue and of the indigenous grower, I consider it desirable to raise substantially the duty on imported betelnuts. I propose to fix the duty (without any surcharge) at the standard rate of 5½ annas a pound, with a preference of 6 pies a pound for British colonies. British colonies even now enjoy a preferential rate of 45 per cent. *ad valorem* against the standard duty of 54 per cent. *ad valorem*. The yield is estimated at Rs. 155 lakhs. I have considered very carefully whether, concurrently with an increase in the customs duty on imported betelnut, I should not reduce the excise on indigenous nuts in view of the fact that the wholesale trade, instead of passing the whole tax on to the consumer, has tended to reduce the price paid to the grower, thereby diminishing the benefit which the latter has derived from the high prices resulting from the cessation of foreign imports during the war. Any such reduction would, however, I am convinced, be absorbed by the wholesale trade and would bring little, if any, benefit to the grower. I am satisfied, moreover, that the increase now proposed in the customs duty on betelnuts renders reduction of the excise less necessary, since wholesale prices ought thereby to remain hereafter at a level which will permit the payment of a reasonable price to the grower. I have, however, been very impressed by the grower's difficulties, which I believe to be rooted in the weakness of his bargaining position *vis a vis* the wholesaler and I think that the grower's interests will be best served by organising the marketing of his products in such a way as to strengthen his position *vis a vis* the wholesale dealer; by improving cultivation methods and, if possible, finding further uses for the nuts; and I propose accordingly to make an annual grant of Rs. 3 lakhs for the purpose of financing measures designed to improve the production and marketing of this crop.

I propose a change in the levy of duty on cotton. At present the customs duty on raw cotton is 1 anna a pound and a further duty of the same amount is levied under the Cotton Fund Ordinance of 1942. The Fund has a sufficient balance to its credit to carry out the purpose for which it was created and it is no longer necessary to aid the Fund by proceeds of the special duty. At the same time, general revenues cannot afford to give up the amount yielded by the duty and I propose to amalgamate the two charges into a consolidated duty of 2 annas a

pound (without any surcharge) which will be leviable wholly under the Indian Tariff Act, the Ordinance being repealed.

I shall bring my indirect taxation proposals to a close with two important changes. The first relates to motor spirit and the second to bullion. It admits of no doubt that, if India is to advance economically and socially, a great improvement in her road communications will be necessary. Village must be joined with village, town with town and producing centres with markets. Although the supply of motor spirit is at present severely restricted, it is not too much to hope that before the next financial year is out both vehicles and petrol will be available in much greater abundance. I propose to encourage the use of road transport by reducing the rate of duty on motor spirit from 15 annas to 12 annas an imperial gallon. This will cost Rs. 165 lakhs of which the share of Customs will be Rs. 120 lakhs.

My last proposal under Customs is in respect of bullion. As the House is aware, the Indian prices of gold and silver bear no sort of parity with world prices. The paucity of imports has, in a large measure, contributed to the present high and artificial prices. With the end of the war, and with the general restoration of normal trade in sight, we may expect the resumption of bullion imports, but we must be prepared to have ready a suitable machinery which will render it unattractive on the part of anyone to indulge in speculation and to hope to reap profits at present levels. I propose, therefore, to provide for the imposition of a specific duty on gold bullion and coin at the rate of Rs. 25 a tola of 180 grains fine. This rate will be varied from time to time by a notification under the Sea Customs Act, in order to attain in an orderly manner a reasonable measure of approximation to world prices. The House will appreciate the difficulties that lie in the way of framing any estimate of the likely imports during next year and the revenue that may result. I am, however, allowing for a revenue of Rs. 1 crore on this account, but the figure is no more than a shot in the dark.

As regards silver, the existing duty is 3 annas an ounce, with a surcharge of 7 1/5 pies. As it is proposed to have a specific duty (without surcharge) on gold, it is appropriate that the rate on silver should be brought reasonably in line, with gold. I accordingly propose to alter the existing rate to 8 annas an ounce, without any surcharge. At this stage I am making no revenue provision on account of this change in the tariff, but this must not be taken as meaning that I am satisfied that there will be no increase in supplies available to the market next year.

All these changes, except that in regard to raw cotton, are being put into immediate effect.

Summary.

I shall now summarise the financial effect of the above proposals. In the field of direct taxation, my income-tax proposals will cost Central Revenues Rs. 21·50 crores, while the changes under customs and excise are expected to yield a net Rs. 5 lakhs. The estimated gap between revenue and expenditure will thus be increased from Rs. 48·71 crores to Rs. 70·16 crores. To bridge a part of this gap, I propose to transfer to revenue Rs. 26·10 crores, being the estimated

balances in the two War Risk Insurance Funds, which sums are transferable to revenue in pursuance of the provisions of the relevant Acts. On the basis of these proposals, next year's deficit comes to Rs. 44·06 crores.

I have come to the end of my story. I have aimed at keeping the revenue at the level necessary to sustain and advance India's economy and I have tried to do this by distributing the burdens and the reliefs evenly and fairly over the various classes of taxpayers. Is it too much to hope that the last budget presented by a British Finance Member will be judged on its merits and will not be rejected on purely political grounds? I humbly believe that my proposals will do something to help my Indian successor, who will shortly be taking over from me and to whom I wish the best of good fortune, to lead India farther along the road to prosperity, happiness and greatness. However that may be, I can assure him of one thing, namely, that he can search the world in vain for a more able, a more loyal or a more devoted body of public servants than those who serve in India's Finance Department and who are predominantly Indian. Brief though my association with them has been, it will always be a source of pride to me that it was my privilege to be their leader, even if for so short a time.

Income-tax (Double Taxation Relief) (Indian States) Rules, 1939—Amendments

Notification No. 3 dated the 6th April 1946.

In exercise of the powers conferred by Section 49A of the Indian Income-tax Act, 1922 (XI of 1922), the Central Government is pleased to direct that the following further amendments shall be made and shall be deemed to have been made with effect from the 1st April 1944, in the Income-tax (Double Taxation Relief) (Indian States) Rules, 1939, namely :—

In the Schedule annexed to the said Rules—

(*a*) under the heading "*Punjab States Agency*"—

(i) the entry "5. Loharu" shall be omitted, and the entries "6. Maler Kotla", "7. Mandi" and "8. Faridkot" shall be renumbered as entries "5. Maler Kotla", "6. Mandi" and "7. Faridkot";

(ii) after entry "7. Faridkot" as renumbered, the entry "8. Tehri Garhwal" shall be inserted.

(*b*) to the entries under the heading "*Deccan States Agency*", the following entries shall be added, namely :—

"8. Kurundwad (Senior).
9. Miraj (Senior)."

(*c*) to the entries under the heading "*Gwalior Agency*", the following entry shall be added, namely :—

"2. Rampur."

(*d*) to the entries under the heading "*Eastern States Agency*", the following entries shall be added, namely :—

"23. Surguja.
24. Bonai.
25. Narsinghpur.
26. Athmahik."

(e) after the heading "*Eastern States Agency*" and the entries thereto, the following heading and entry shall be inserted, namely :—

"*Rajputana States Agency.*

1. Bundi".

Excess Profits Tax (Post-War Refunds) Rules, 1942.

Notification No. 1 dated the 6th April 1946.

In exercise of the powers conferred by sub-section (3) of Section 10 of the Indian Finance Act, 1942 (XII of 1942), and by that sub-section read with sub-section (5) of Section 2 of the Excess Profits Tax Ordinance, 1943 (No. XVI of 1943), the Central Government is pleased to direct that the following further amendment shall be made in the Excess Profits Tax (Post-war Refunds) Rules, 1942, namely :—

In Form E.P. 4-17, appended to the said Rules, the word "Civil" wherever it occurs, shall be omitted.

Indian Income-tax Rules; 1922—Amendments.

Notification No. 14-Camp. dated the 2nd March 1946.

In exercise of the powers conferred by sub-section (1) of Section 59 of the Indian Income-tax Act, 1922 (XI of 1922), the Central Board of Revenue directs that the following further amendment shall be made in the Indian Income-tax Rules, 1922, the same having been previously published as required by sub-section (4) of the said section, namely :—

In the statement set out below Rule 8 of the said Rules, under the head "III. Machinery and plant" and sub-heading "(2) Special rates to be applied to the whole of the machinery and plant used in the following concerns :—"against the letter "B"—

(1) In item (XXX) after the words "Iron and Steel Industry" an asterisk * shall be inserted and in the column headed "Remarks" against this item an asterisk and words "*Replacement of rolling mill rolls will be allowed as revenue expenditure" shall be inserted ;

(2) After item (XXXIV) the following item shall be inserted, namely :—

"(XXXV) Manufacture of pottery and other clay products."

Auditor's Certificates Rules, 1932—Amendments.

Notification No. 1A (9)/45 dated the 9th March 1946.

In exercise of the powers conferred by sub-section (2) of Section 144 of the Indian Companies Act, 1913 (VII of 1913), the Central Government is pleased to direct that the following further amendment shall be made in the Auditor's Certificates Rules, 1932, the same having been previously published as required by the said sub-section, namely :—

In sub-rule (1) of Rule 16 of the said Rules, after the word "Accountants" the following shall be inserted namely :—

"or by reason of occupation of Burma or the Far East by the enemy."

Income Tax Reports.

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Income-tax Establishments.

Notification No. 2 dated the 30th March 1946.

In pursuance of sub-section (4) of Section 5 of the Indian Income-tax Act, 1922 (XI of 1922), the Central Board of Revenue directs that with effect from the 1st April 1946, the following further amendment shall be made in the schedule appended to its notification No. 58-Income-tax, dated the 15th July 1939, namely :—

In the said Schedule under the sub-head "IV—United Provinces and Central Provinces and Berar" for the Ranges and Income-tax Circles specified against them, the following Ranges and Income-tax Circles shall be substituted, namely :—

Lucknow—
(1) Lucknow
(2) Bareilly
(3) Fyzabad
(4) Gonda
(5) Sitapur
(6) Moradabad
(7) Jhansi

Agra—
(1) Agra
(2) Aligarh
(3) Saharanpur
(4) Dehradun
(5) Meerut
(6) Military Circle, Meerut

Cawnpore—
(1) Special Income-tax *cum* Excess Profits Tax Circle, Cawnpore
(2) Cawnpore
(3) Fatehgarh
(4) Allahabad
(5) Central Salary Circle, Allahabad

Benares—
(1) Benares
(2) Azamgarh
(3) Gorakhpur

Nagpur—
(1) Income-tax *cum* Excess Profits Tax Circle, Nagpur
(2) Akola
(3) Khamgaon
(4) Nagpur
(5) Wardha
(6) Yeotmal
(7) Amraoti
(8) Salary Circle, Nagpur

Jubbulpore—
(1) Jubbulpore
(2) Saugor
(3) Chhindwara
(4) Raipur
(5) Khandwa

Notification No. 5 dated the 13th April 1946.

In exercise of the powers conferred by sub-section (3) of Section 5 of the Indian Income-tax Act, 1922 (XI of 1922), the Central Government is pleased to cancel the notification of the Government of India in the Finance Department (Central Revenues) No. 28-Income-tax, dated the 15th April 1939.

Notification No. 4 dated the 13th April 1946.

In pursuance of sub-section (4) of Section 5 of the Indian Income-tax Act, 1922 (XI of 1922), the Central Board of Revenue directs that the following further amendment shall be made in its notification No. 58-Income-tax, dated the 15th July 1939, namely :—

Income-tax Establishments.

Notification No. 2-D dated the 20th April 1946.

In exercise of the powers conferred by sub-section (6) of Section 5 of the Indian Income-tax Act, 1922 (XI of 1922), the Central Board of Revenue directs that the following further amendment shall be made in its Notification No. 19-Income-tax, dated the 1st April 1939, namely :—

In the Schedule appended to the said notification, after Serial No. 62, the following shall be inserted, namely :—

"62-A	Persons in the payment of Force 136, Dholpur House, New Delhi.	do.	do.	do.	do.

Notification No. 19 dated the 30th April 1946.

In exercise of the powers conferred by sub-section (2) of Section 5 of the Indian Income-tax Act, 1922 (XI of 1922) and in supersession of all previous notifications in this behalf, the Central Government is pleased to appoint with effect from the 1st May 1946 the persons mentioned in column 2 of the Schedule appended hereto to be the Commissioners of Income-tax for the Areas specified in the corresponding entry in column 3 thereof.

SCHEDULE

S. No.	Name	Area
1	Dewan Bahadur R. Varadachari	Bombay City and Bombay Suburban District
2	Rao Bahadur V. D. Muzumdar	Calcutta City and the 24 Parganas and Howrah-Districts
3	Mr. Abdul Qadir	Punjab, North West Frontier Provinces and Delhi
4	Mr. P. C. Padhi	Province of Madras
5	Mr. A. K. Roy	United Provinces and Ajmer Merwara
6	Mr. Sardar Bahadur	Province of Bombay (excluding Bombay City and Bombay Suburban District)
7	Rai Sahib B. K. Mukerji	Bengal (Excluding Calcutta City and the 24 Parganas and Howrah District)
8	Rai Sahib P. D. Swaminadha Mudaliar	Central Provinces & Berar
9	Khan Bahadur Nazar Mohommad Khan	Bihar and Orissa
10	Mr. L. W. Thompson	Sind and Baluchistan
11	Mr. G. D. Bagri	Assam.

Notification Relating to Refund of Tax Paid under Finance Acts.

Notification No. 9 dated the 4th May 1946.

In exercise of the powers conferred by sub-section (7) of Section 8 of the Indian Finance Act, 1942 (XII of 1942), sub-section (7) of Section 5 of the Indian Finance Act, 1943 (VIII of 1943), sub-section (7) of Section 6 of the Indian Finance Act, 1944, and sub-section (7) of Section 7 of the Indian Finance Act, 1945, the Central Government is pleased to fix the 1st day of March 1947 as the date on which the amounts funded for the assessees' benefit under the said sub-sections shall be paid to the assessees.

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Excess Profits Tax (Post War Refunds) Rules, 1942—Amendment.

Notification No. 2 dated the 29th June, 1946.

In exercise of the powers conferred by sub-section (3) of Section 10 of the Indian Finance Act, 1942 (XII of 1942), read with sub-section (5) of Section 2 of the Excess Profits Tax Ordinance, 1943 (No. XVI of 1943), the Central Government is pleased to direct that the following further amendment shall be made in the Excess Profits Tax (Post War Refunds) Rules, 1942, namely :—

In Form E. P. 4-17, appended to the said Rules, after the word "that" in the first line of paragraph 2, the words "in the case of plant and machinery" shall be inserted.

Indian Income-tax Rules, 1922—Amendment.

Notification No. 21 dated the 20th July, 1946.

In exercise of the powers conferred by sub-section (1) of Section 59 of the Indian Income-tax Act, 1922, the Central Board of Revenue directs that the following further amendment shall be made in the Indian Income-tax Rules, 1922, the same having been previously published as required by sub-section (4) of the said section, namely :—

After rule 46 of the said Rules, the following rule shall be inserted, namely :—

"47. For the purposes of clauses (xiii) and (xiv) of sub-section (2) of Section 10 of the Act, the 'prescribed authority' shall be the Council of Scientific and Industrial Research, the Imperial Council of Agricultural Research, or the Indian Research Fund Association, as may be appropriate to the nature of the Scientific Research in question."

Notification No. 6-D dated the 27th July, 1946.

In exercise of the powers conferred by sub-section (1) of Section 59 of the Indian Income-tax Act, 1922 (XI of 1922), the Central Board of Revenue directs that the following further amendment shall be made in the Indian Income-tax Rules, 1922, the same having been previously published as required by sub-section (4) of the said section, namely :—

In rule 45 of the said Rules, after entry 6 the following entry shall be inserted, namely :—

"7. Senior All-India Diploma in Commerce awarded by the All-India Board of Technical Studies in Commerce, Business Administration and Economics of the All-India Council for Technical Education provided that the diploma-holder took 'Advanced Accountancy and Auditing' as his optional subject for the diploma course."

Income-tax Appellate Tribunal (Destruction of Records) Rules, 1946.

Notification No. F. 27/46-ITAT dated the 22nd July, 1946.

In exercise of the powers conferred by Section 3 of the Destruction of Records Act, 1917 (V of 1917), the Central Government is pleased to make the following rules, namely :—

1. These rules may be called the Income-tax Appellate Tribunal (Destruction of Records) Rules, 1946.

2. The records and registers of the Income-tax Appellate Tribunal specified in Column 1 of the following table may be destroyed at the end of the period specified in the corresponding entry in Column 2 thereof.

Description of records or registers (1)	Period (2)
1. *Appeal Records.*	
(i) Order Sheet, memo of appeal, treasury receipt for the Tribunal's fee, Tribunal's order and order if any for refund of fee paid in excess.	12 years from the date of the Tribunal's final order in the appeal.
(ii) Documents other than those referred to in (i).	3 years from the date of the Tribunal's final order in the appeal.
2. *Reference Application Records.*	
(i) Copies of judgments of the High Court or the Privy Council, if any.	12 years from the date of the Tribunal's final order in the connected appeal.
(ii) Documents other than those referred to in (i).	3 years from the date of the Tribunal's order in the connected appeal.
3. Register of Appeals, Register of E. P. T. Appeals and Disposal Register.	3 years from the latest date of disposal of appeal in the register.
4. Register of Reference Applications.	3 years from the latest date of disposal of application in the register.

Income-tax Establishments.

Notification No. 16 dated the 23rd May, 1946.

In pursuance of sub-section (4) of Section 5 of the Indian Income-tax Act, 1922 (XI of 1922), the Central Board of Revenue directs that the following further amendment shall be made in the Schedule appended to its notification No. 58-Income-tax, dated the 15th July, 1939, namely :—

In the said Schedule under the sub-head "II-Bombay, Sind and British Baluchistan"—

(i) for entry No. 12 against 'Bombay C Range' the following entry shall be substituted, namely :—

(12) Bombay Suburban District.

(ii) after entry No. (12) against Belgaum Range, the following entry shall be added, namely :—

(13) Thana District.

Notification No. 18 dated the 22nd June, 1946.

In pursuance of sub-section (4) of Section 5 of the Indian Income-tax Act, 1922 (XI of 1922), the Central Board of Revenue directs that with effect from the 15th June 1946, the following further amendment shall be

made in its notification No. 58-Income-tax, dated the 15th July, 1939, namely :—

In the Schedule appended to the said notification under the sub-head "V-Punjab, North-West Frontier Province and Delhi" for the existing Ranges and Income-tax Circles mentioned against them, the following Ranges and Income-tax Circles shall be substituted, namely :—

Range	Income-tax Circles
Lahore	(1) Lahore. (2) Salaries Circle, Lahore. (3) Lyallpur. (4) Gujranwala. (5) Gujrat. (6) Sargodha. (7) Montgomery. (8) Multan. (9) Jhelum.
Rawalpindi	(1) Rawalpindi. (2) Peshawar. (3) Nowshera. (4) Dehra Ismail Khan.
Amritsar	(1) Amritsar. (2) Jullundur. (3) Gurdaspur. (4) Sialkot. (5) Hoshiarpur.
Delhi	(1) Delhi. (2) Salary Circle, Delhi. (3) Hissar. (4) Rohtak. (5) Ambala. (6) Simla. (7) Ludhiana. (8) Ferozpur. (9) Karnal.

Notification No. 14 dated the 1st June, 1946.

In pursuance of sub-section (4) of Section 5 of the Indian Income-tax Act, 1922 (XI of 1922), the Central Board of Revenue directs that the following further amendment shall be made in the Schedule appended to its notification No. 58-Income-tax dated the 15th July, 1939, namely :—

In the said Schedule—

(i) for the sub-head "II Bombay, Sind, British Baluchistan and Ajmer-Merwara" *substitute* "II Bombay, Sind and British Baluchistan."

(ii) Under the sub-head "II Bombay, Sind and British Baluchistan" entry No. (9) against Ahmedabad Range shall be deleted.

(iii) For the sub-head "IV United Provinces and Central Provinces and Berar" *substitute* "IV United Provinces, Central Provinces, Berar and Ajmer-Merwara".

(iv) Under the sub-head "IV United Provinces, Central Provinces, Berar and Ajmer-Merwara," after entry No. (9) against "Agra Range" the following entry shall be added, namely :—"(10) Ajmer-Merwara".

Notification No. 22 dated the 12th July, 1946.

In pursuance of sub-section (4) of Section 5 of the Indian Income-tax Act, 1922 (XI of 1922), the Central Board of Revenue directs that with effect from the 12th July, 1946, the following further amendment shall be made in the schedule appended to its notification No. 58—Income-tax, dated the 15th July, 1939, namely :—

In the said Schedule under the sub-head "IV—United Provinces and Central Provinces and Berar" for the Ranges Lucknow, Agra, Cawnpore

and Benares and the Income-tax Circles specified against them, the following Ranges and Income-tax Circles shall be substituted, namely :—

Cawnpore—(1) Cawnpore. (2) Special Income-tax *cum* Excess Profits Tax Circle, Cawnpore. (3) Fatehgarh.

Lucknow—(1) Lucknow. (2) Sitapur. (3) Bareilly. (4) Gonda. (5) Fyzabad. (6) Allahabad. (7) Central Circle, Allahabad.

Meerut—(1) Meerut. (2) Military Circle, Meerut. (3) Saharanpur. (4) Dehradun, (5) Moradabad.

Agra—(1) Agra. (2) Aligarh. (3) Jhansi. (4) Ajmer-Merwara.

Benares—(1) Benares. (2) Azamgarh. (3) Gorakhpur.

Corrigendum.

Notification No. 20 dated the 13th July, 1946.

In the notification of the Central Board of Revenue No. 16—Income-tax dated the 23rd May, 1946, for the figure '12' wherever it occurs in amendment (i) read '7'.

Auditor's Certificates Rules, 1932.

Notification No. 7-A (1)/46 dated the 22nd June, 1946.

In pursuance of clause (iii) of sub-clause (a) of clause (3) of rule 22 and clause (b) of rule 41 of the Auditor's Certificates Rules, 1932, the Central Government is pleased to recognise the following examinations as equivalent to the Intermediate Examination of a University constituted by law in British India or British Burma or of the University of Mysore or of the Osmania University, namely :—

1. The Intermediate Examination of any Indian University incorporated by a law for the time being in force, other than those mentioned in rules 22 and 41 of the said Rules or of a Board of Intermediate Examination in India established by a resolution of Government.
2. The First Year Examination of the three-year degree course of the Delhi University.
3. The Pre-Engineering Examination of the Delhi Polytechnic.
4. The Final Examination of the Government Commercial Institute, Calcutta.
5. The Pre-Medical Examination of the Delhi University.
6. The Cambridge Higher School Certificate Examination.
7. The Examination for the Diploma of Licentiate of Arts of St. Andrews University.
8. The Higher Oxford Certificate Examination with a combination of subjects considered by the Academic Council to be equivalent to that prescribed for the Intermediate (Arts and Science) Examination of the Nagpur University.
9. The Intermediate Examination (Arts) of the University of London.

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Auditor's Certificates Rules, 1932—Amendments.

Notification No. 1-A (1)/46 dated the 27th July, 1946.

In exercise of the powers conferred by sub-section (2) of Section 144 of the Indian Companies Act, 1913 (VII of 1913), the Central Government is pleased to direct that the following further amendment shall be made in the Auditor's Certificates Rules, 1932, the same having been previously published as required by the said sub-section, namely :—

In rule 21 of the said Rules, clause (b) shall be re-lettered as clause (c), and before clause (c), as so re-lettered the following clause shall be inserted, namely :—

"(b) has passed the All-India Senior Diploma in Commerce Examination held by the All-India Board of Commercial Studies, Delhi, with Auditing as a special subject, or."

Notification No. 1-A (3)/46 dated the 27th July, 1946.

In exercise of the powers conferred by sub-section (2) of Section 144 of the Indian Companies Act, 1913 (VII of 1913), the Central Government is pleased to direct that the following further amendment shall be made in the Auditor's Certificates Rules, 1932, the same having been previously published as required by the said sub-section, namely :—

Rule 77 of the said Rules shall be omitted.

Notification No. 1-A (2)/46 dated the 3rd August, 1946.

In exercise of the powers conferred by sub-section (2) of Section 144 of the Indian Companies Act, 1913 (VII of 1913), the Central Government is pleased to direct that with effect from the 1st May 1947, the following further amendment shall be made in the Auditor's Certificates Rules, 1932, the same having been previously published as required by the said sub-section, namely :—

For clause (ii) of rule 25 of the said Rules, the following clause shall be substituted, namely :—

"(ii) has either completed such period of service as an articled clerk or as an audit clerk or partly as an articled clerk and partly as an audit clerk as is required under rule 36 for enrolment on the Register or is serving the last twelve months of such period or is eligible for such enrolment under clause (d) of rule 36."

Notification No. 1-A (5)/45 dated the 3rd August, 1946.

In exercise of the powers conferred by sub-section (2) of Section 144 of the Indian Companies Act, 1913 (VII of 1913), the Central Government is pleased to direct that the following further amendment shall be made in the Auditor's Certificates Rules, 1932, the same having been previously published as required by the said sub-section, namely :—

In the proviso to rule 22 of the said Rules—

1. For clause (1) the following clause shall be substituted, namely :—

"(1) a candidate who produces a certificate in the form given in appendix 4 in respect of a period of study prior to 1946-47, or for 1946-47 if he has entered into service as an audit clerk before the 1st October 1945, shall be eligible for admission on passing the Intermediate or equivalent examination; and"

2. In clause (2)—

(i) after the words and figures "to be held in 1947" the word and figures "and 1948" shall be inserted; and

(ii) in sub-clause (iii), for the words "has appeared and failed at" the words "was admitted to" shall be substituted.

Notification No. 1-A (6)/45 dated the 3rd August, 1946.

In exercise of the powers conferred by sub-section (2) of Section 144 of the Indian Companies Act, 1913 (VII of 1913), the Central Government is pleased to direct that the following further amendment shall be made in the Auditor's Certificates Rules, 1932, the same having been previously published as required by the said sub-section, namely:—

For the proviso to rule 19 of the said Rules, the following proviso shall be substituted, namely:—

"Provided as follows:—

(a) any period served between the 3rd September 1939 and the 30th September 1946 (both dates inclusive) under articles for any of the Institutes or Societies of Chartered Accountants in England and Wales, Scotland or Ireland or the Society of Incorporated Accountants and Auditors, London, shall be set off against the practical training prescribed under rule 36;

(b) the passing between the said dates of the Intermediate or Final Examination of any of the aforesaid Institutes or Societies shall be treated as equivalent to the passing of the First or Final Examination respectively held under these Rules."

Notification No. 1-A (3)/45 dated the 7th September, 1946.

In exercise of the powers conferred by sub-section (2) of Section 144 of the Indian Companies Act, 1913 (VII of 1913), the Central Government is pleased to direct that the following further amendments shall be made in the Auditor's Certificates Rules, 1932, the same having been previously published as required by the said sub-section, namely:—

In the said Rules—

I. In clause (a) of rule 21, after the words "Osmania University" the words "or of the University of Travancore" shall be inserted.

II. In rule 36—

(1) sub-clauses (iii) and (iv) of clause (a) shall be renumbered as sub-clauses (iv) and (v), respectively, and before sub-clause (iv) as so re-numbered, the following sub-clause shall be inserted, namely:—

"(iii) in the case of a person who has passed the degree Examination of any of the Universities mentioned in clause (b) of rule 2 and has either taken Accounting, Auditing and Mercantile or Commercial Law among his subjects for the degree course, or has secured a minimum of 60 per cent. of the total marks...........3 years";

(2) in sub-clause (iv) of clause (a) as so re-numbered, for the words, "a graduate" the words "any other graduate" shall be substituted;

(3) sub-clauses (ii) and (iii) of clause (b) shall be re-numbered as sub-clauses (iii) and (iv), respectively, and before sub-clause (iii) as so re-numbered, the following sub-clause shall be inserted, namely:—

"(ii) in the case of a person referred to in sub-clause (iii) of clause (a)...........6 years";

(4) in sub-clause (iii) of clause (b) as so re-numbered, for the words "a graduate" the words "any other graduate" shall be substituted;

(5) in clause (c), for the words, brackets and figures "or sub-clause (ii)" the words, brackets and figures "sub-clause (ii) or sub-clause (iii)" shall be substituted;

(6) in clause (5) of the proviso, for the words, brackets and figures "sub-clauses (iii) and (iv)" the words, brackets and figures "sub-clauses (iv) and (v)" shall be substituted.

Income-tax Rules, 1922—Amendments.

Notification No. 25 dated the 17th August, 1946.

In exercise of the powers conferred by sub-section (1) of Section 59 of the Indian Income-tax Act, 1922 (XI of 1922), the Central Board of Revenue directs that the following further amendments shall be made in the Indian Income-tax Rules, 1922, the same having been previously published as required by sub-section (4) of the said section, namely:—

In the "Form of return of total income and total world income for individuals, Hindu undivided families, companies, local authorities, firms and other associations of persons required under sub-section (1) or (2) of Section 22", set forth in sub-rule (1) of rule 19 of the said Rules—

(1) in the Statement under Part IV,—

(a) in item "Depreciation allowable as shown in Part V of this Return—*See note* 17(c)" for the figures, letter, and brackets "17(c)" the figures, letter and brackets "17(d)" shall be substituted; and

(b) after the above item as so amended, the following item shall be inserted, namely:—

"*Scientific Research Expenditure* (if not charged in arriving at the above figure of profit).

(i) Any expenditure (not in the nature of capital expenditure) laid out or expended on scientific research related to the business—*See note* 17(c). Give details.

(ii) Any sum paid to an approved scientific research association or an approved university, college or other institution for such scientific research —*See note* 17(c). Give details.

(iii) Any expenditure of a capital nature on scientific research related to the business admissible under Section 10 (2) (xiv) of the Act—*See note* 17(c). Give details";

(2) in the Statement under Part V,—

(a) for the marginal note "[*See note* 17(c)]" the marginal note "[*See note* 17(d) and 17(e)]" shall be substituted;

(b) in the heading of column 2 for the words, figures, letter and brackets "[*See* note 17(c)]" the words, figures, letter and brackets "[*See* note 17(d)]" shall be substituted;

(c) in the heading of column 3 the mark "†" shall be placed immediately before the word "Capital"; and

(d) at the end of the statement to the existing notes the following further note shall be added, namely:—

"†(3) Capital expenditure on new machinery or plant or new buildings erected should be shown separately and in the Remarks column against each such entry, it should be indicated that initial depreciation is claimed.";

(3) In the Statement under Part VI for the existing heads at the bottom, the following heads shall be substituted, namely:—

"Total income from property..

Less (i) Claim for irrecoverable rent (Give details separately).

(ii) Income from property erected during the period 1st April 1946 to 31st March 1948.

Net income from property carried to Part I of the return..............................."; and

(4) In the "Notes for guidance in filling up Return Form No. I. T. 11"—

(a) to Note 1-A, the following shall be added, namely :—

"Super-tax in these cases should be calculated at the rates and in the manner specified in the annual Finance Act.";

(b) in Note 17—

(i) after paragraph (b) the following new paragraph shall be inserted, namely :—

"(c) Under Section 10 (2) (xii), (xiii) and (xiv) of the Act, revenue expenditure incurred by the assessee on scientific research related to a business or to the class of business carried on and sums paid to research associations or institutions will be allowed in the assessment of the profits of the year in which the expenses were incurred. Capital expenditure on scientific research will be allowed in five consecutive equal instalments and allowance will be given also in respect of such expenditure incurred not more than three years before the commencement of the business. Any expenditure on scientific research incurred in the previous year for the assessment year 1945-46 is admissible as a deduction in the assessment year 1946-47, but not in any subsequent year of assessment";

(ii) the existing paragraph "(c)" shall be re-lettered as "(d)"; and

(iii) after paragraph "(d)" as so re-lettered the following paragraph shall be added, namely :—

"(e) Under Section 10 (2) (vi) of the Act special initial depreciation will be admissible in respect of new buildings, plant and machinery. In the case of buildings, the rate is 10 per cent. of the cost except in the case of buildings erected in the period 1st April 1946 to 31st March 1948 for which it is 15 per cent. In the case of plant and machinery the rate is 20 per cent. The allowance will not be deducted in computing the written down value".

Income-tax Establishments.

Notification No. 24 dated the 10th August, 1946.

In pursuance of sub-section (4) of Section 5 of the Indian Income-tax Act, 1922 (XI of 1922), the Central Board of Revenue directs that with effect from the 15th August 1946, the following further amendment shall be made in its notification No. 58-Income-tax, dated the 15th July 1939, namely :—

In the Schedule appended to the said notification under the sub-head "VI-Bihar and Orissa" for the existing Ranges and Income-tax Circles mentioned against them the following Ranges and Income-tax Circles shall be substituted, namely :—

Patna.—(1) Patna. (2) Bhagalpur. (3) Special Circle, Patna. (4) Special Circle, Cuttack. (5) Gaya. (6) Shahabad-Palamau Circle, Arrah. (7) Santhal Parganas. (8) Hazaribagh. (9) Purnea.

Purulia.—(1) Ranchi-Manbhum Sadar. (2) Singhbhum-Sambalpur (3) Cuttack-Balasore. (4) Ganjam-Puri-Koraput. (5) Dhanbad.

Muzaffarpur.—(1) Muzaffarpur. (2) Saran. (3) Champaran. (4) Darbhanga. (5) Monghyr.

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Income-tax Establishments.

Notification No. 26 dated the 15th August, 1946.

In pursuance of sub-section (4) of Section 5 of the Indian Income-tax Act, 1922 (XI of 1922), the Central Board of Revenue directs that the following further amendment shall be made in its notification No. 58 Income-tax, dated the 15th July 1939, namely :—

In the Schedule appended to the said notification under the sub-head "I-Madras" for the existing Ranges and Income-tax Circles mentioned against them, the following Ranges and Income-tax Circles shall be substituted, namely :—

Range	Income-tax Circles
BEZWADA	1. Vizianagaram
	2. Vizagapatam
	3. Cocanada
	4. Rajahmundry
	5. Ellore
	6. Masulipatam
	7. Bezwada I
	8. Bezwada II
	9. Guntur
	10. Tenali
	11. Bapatla
	12. Kurnool
	13. Bellary
MADRAS 'A'	1. Madras II
	2. Madras V
	3. Madras VI
	4. Salem I
	5. Salem II
	6. Madras (Special) Central
	7. Madras (Special) South
	8. Nellore I
	9. Nellore II
MADRAS 'B'	1. Madras I
	2. Madras III
	3. Madras IV
	4. Conjeevaram
	5. Cuddalore
	6. Vellore
MADRAS 'B' (*contd.*)	7. Chittoor
	8. Cuddappa
	9. Anantapur
	10. Madras (Special) North
	11. Madras (Special) East
COIMBATORE	1. Mangalore
	2. Calicut
	3. Palghat
	4. Coimbatore I
	5. Coimbatore II
	6. Ootacamund
	7. Coimbatore (Special)
	8. Coorg.
TRICHINOPOLY	1. Negapatam
	2. Tanjore
	3. Trichinopoly I
	4. Trichinopoly II
	5. Dindigul
	6. Madura (North)
	7. Madura (South)
	8. Karaikudi I
	9. Karaikudi II
	10. Virudhunagar
	11. Tinnevelly
	12. Tuticorin
	13. Madura (Special)
	14. Erode
	15. Erode (Special)

Indian Income-tax Rules, 1922—Amendments.

Notification No. 27 dated the 21st September, 1946.

In exercise of the powers conferred by sub-section (1) of Section 59 of the Indian Income-tax Act, 1922 (XI of 1922), the Central Board of Revenue directs that the following further amendments shall be made in the Indian Income-tax Rules, 1922, the same having been previously published as required by sub-section (4) of the said section, namely :—

In the statement set out in rule 8 of the said Rules, under the head "III Machinery and Plant"—

(1) In sub-head (2) item (xxvii) of group B shall be omitted.

(2) To sub-head (3) the following shall be added, namely :—

" T-Glass manufacturing concerns*.		* Replacement of Direct Fire Glass melting Furnaces will be allowed as revenue expenditure.
(i) Recuperative and Regenerative Glass Melting furnaces.	20%	
(ii) Other plant and machinery including machinery for the manufacture of Vacuum tubes and Vacuum bulbs.	10% "	

Income-tax Establishments.

Notification No. 19-D dated the 12th October, 1946.

In pursuance of sub-section (4) of Section 5 of the Indian Income-tax Act, 1922 (XI of 1922), and in supersession of the Board's Notification No. 3-Camp-D, Income-tax, dated the 10th November 1945, the Central Board of Revenue directs that the Appellate Assistant Commissioner of Income-tax, Andaman and Nicobar Islands shall perform his functions in respect of all persons and of all incomes assessed to income-tax and/or super-tax in the said Islands.

Notification No. 29 dated the 12th October, 1946.

In pursuance of sub-section (4) of Section 5 of the Indian Income-tax Act, 1922 (XI of 1922), the Central Board of Revenue directs that with effect from the 15th October 1946, the following further amendment shall be made in its Notification No. 58-Income-tax, dated the 15th July 1939, namely :—

In the Schedule appended to the said notification under the sub-head "II—Bombay, Sind and British Baluchistan" for Bombay 'A', Bombay 'B', Bombay 'C' and Bombay 'D' Ranges and Income-tax Circles mentioned against them, the following Ranges and Income-tax Circles shall be substituted, namely :—

Bombay "A" Range	(1) A-I Ward.
	(2) A-II "
	(3) A-III "
	(4) A-IV "
	(5) A-V "
	(6) D-I "
	(7) D-II "
	(8) G "
	(9) M "
Bombay "B" Range	(1) Companies Circle I (all sections).
	(2) " " II "
	(3) " " III "
	(4) " " IV "
	(5) Air Force Circle, Bombay.
Bombay "C" Range	(1) B-I Ward.
	(2) B-II "
	(3) B-III "
	(4) C-I "
	(5) C-II "
	(6) C-III "
	(7) C-IV "
Bombay "D" Range	(1) Central Section I
	(2) " " II
	(3) " " III
	(4) " " IV
	(5) " " V
	(6) " " VI
Bombay D Range (*contd.*)	(7) Central Section VII
	(8) " " VIII
	(9) " " IX
	(10) " " X
	(11) " " XI
	(12) " " XII
	(13) E Ward.
Bombay "E" Range	(1) Bombay Circle I
	(2) " " II
	(3) " " III
	(4) " " IV
	(5) " " V
	(6) " " VI
	(7) " " VII
	(8) " " VIII
	(9) " " IX
	(10) " " X
	(11) " " XI
	(12) " " XII
	(13) " " XIII
	(14) " " XIV
	(15) " " XV
	(16) " " XVI
	(17) Bombay Suburban District.
	(18) Salaries Section I
	(19) " " II
	(20) Bombay Refund Circle.

Auditor's Certificates Rules, 1932—Amendments.

Notification No. 1-A (4)/46 dated the 28th September, 1946.

In exercise of the powers conferred by sub-section (2) of Section 144 of the Indian Companies Act, 1913 (VII of 1913), the Central Government is pleased to direct that the following further amendments shall be made in the Auditor's Certificates Rules, 1932, the same having been previously published as required by the said sub-section, namely :—

A. In the said Rules—

I. To clause (2) of the proviso to rule 41, the following shall be added, namely :—

"the All-India Senior Diploma in Commerce Examination held by the All-India Board of Commercial Studies, Delhi, with Auditing as a special subject."

II. In sub-rule (1) of rule 49B, for the word "six" the word "eight" shall be substituted.

B. In the Note to item (5) in Appendix 3 to the said Rules—

I. In clause (d), the word "or" where it last occurs, shall be omitted.

II. In clause (e), after the word "Auditors" the word "or" shall be inserted.

III. After clause (e) the following clause shall be inserted, namely :—

"(f) A title indicating membership of any Institution as may be recognised by the Central Government."

Notifications under Auditor's Certificates Rules, 1932.

Notification No. 7-A (1)/45 dated the 28th September, 1946.

In pursuance of clause (iii) of sub-clause (a) of clause (3) of rule 22 and clause (b) of rule 41 of the Auditor's Certificates Rules, 1932, the Central Government is pleased to direct that the following amendment shall be made in the notification of the Government of India in the Department of Commerce, No. 7-A (1)/45, dated the 22nd June, 1946, namely :—

In the said Notification, after item 9, the following item shall be inserted, namely :—

"10. The Commercial Diploma Examination of the Board of High School and Intermediate Education. United Provinces."

Notification No. 9-A (6)/46 dated the 28th September, 1946.

In pursuance of sub-rule (3) of rule 49 of the Auditor's Certificates Rules, 1932, the Central Government is pleased to direct that the following amendment shall be made in the notification of the Government of India in the Department of Commerce No. 9-A (4)/44, dated the 1st July, 1944, namely :—

In the list of Members in the said notification, under the head "Nominated" and the sub-head "Officials," entry No. 1, relating to the Honourable Dr. Sir Muhammad Azizul-Haque, shall be omitted.

Restricted Certificates Rules, 1932—Amendments.

Notification No. 1-A (4)/46 (i) dated the 28th September, 1946.

In exercise of the powers conferred by sub-section (2) of Section 3 of the Indian Companies (Amendment) Act, 1930 (XIX of 1930), the Central Government is pleased to direct that the following further amendments

shall be made in the Restricted Certificates Rules, 1932, the same having been previously published as required by the said sub-section, namely :—

In the Note to item (5) in the Appendix to the said Rules—

(1) In clause (d), the word " or " where it last occurs, shall be omitted;

(2) in clause (e), after the word " Auditors " the word " or " shall be inserted; and

(3) after clause (e) the following clause shall be inserted, namely :—

" (f) A title indicating membership of any Institution as may be recognised by the Central Government."

Excess Profits Tax (Post-War Refunds) Rules, 1942—Amendments.

Notification No. 3 dated the 26th October, 1946.

In exercise of the powers conferred by sub-section (3) of Section 10 of the Indian Finance Act, 1942 (XII of 1942), read with sub-section (5) of Section 2 of the Excess Profits Tax Ordinance, 1943 (XVI of 1943), the Central Government is pleased to direct that the following further amendments shall be made in the Excess Profits Tax (Post-war Refunds) Rules, 1942, namely :—

I. In the said Rules, after rule 8, the following rule shall be inserted, namely :—

" 9. (1) An application for refund of a deposit made under the Finance Act or the Ordinance shall be made in Form E.P. 4-21 to the Excess Profits Tax Officer, and the Excess Profits Tax Officer shall refund the amount deposited to the person who made the deposit.

Provided that—

(i) in the case of an individual who, at the time when the deposit is refundable, is dead, refund shall be made to the person, who, under a letter of administration, probate or succession certificate, is entitled thereto;

(ii) in the case of a Company which, at the time when the deposit is refundable, is in course of winding up, refund shall be made to the Liquidator of the Company;

(iii) in the case of a Hindu undivided family which, at the time when the deposit is refundable, has been disrupted, the refund shall be made to the person or persons to whom the deposit was assigned upon such disruption;

(iv) in the case of a firm the constitution of which, at the time when the deposit is refundable, is different from its constitution during the chargeable accounting period in respect of which the deposit was made, refund shall be made to the firm as constituted when the refund is due;

(v) in the case of a firm, which, at the time when the deposit is refundable, is no longer in existence, refund shall be made jointly to the persons who were partners in the firm during the chargeable accounting period in respect of which the deposit was made, or to any person jointly nominated by them to receive the refund, with the substitution in the case of a deceased partner of the administrator or other legal representative.

Provided further that, if the identity of the person entitled under the preceding provisions to receive a refund is in dispute or if any substantial question of title is, in the opinion of the Excess Profits Tax Officer, involved; such Officer may require the production of an order of the Competent Civil Court determining the person entitled to receive the refund or any part thereof.

(2) Any refund made in accordance with sub-rule (1) shall be deemed to be a full and valid discharge of the liability of the Central Government under the Finance Act or Ordinance, and the person to whom the refund is made shall be responsible for any liability arising out of a claim by any other person in respect of such refund."

II. In the Forms appended to the said Rules, after Form E.P. 4-17, the following Form shall be inserted, namely :—

"FORM E.P. 4-21.

EXCESS PROFITS TAX.

Application for the Refund of deposits made under the provisions of Section 10, Finance Act, 1942, and Section 2 of Excess Profits Tax Ordinance, 1943.

To

The Excess Profits Tax Officer, at..

The following sums deposited by..
....................with the Government of India under the provisions of Section 10 of the Finance Act, 1942, and/or Section 2 of the Excess Profits Tax Ordinance, 1943, are refundable not later than the....................day of ....194 .

SCHEDULE OF SUMS DEPOSITED.

Chargeable Accounting Period.		Sums deposited Rs.	Date (s) on which sums deposited
Commencing	Ending		

I/We do hereby pray for a refund of the amount together with interest thereon, under the provisions of rule 9 of the Excess Profits Tax (Post-war Refunds) Rules, 1942.

I/We hereby agree that the payments authorised may be treated as provisional subject to readjustment in due course on the basis of audited figures, and I/We hereby undertake to repay the excess amount, if any, refunded by Government either in respect of the sum deposited by me/us, or in respect of the relative interest thereon.

I/We further agree that if any claim is made by any other person in respect of the deposit, refund of which is claimed hereby, I/We shall be responsible therefor.

Signature and Address of each claimant.

Signature	Address	Capacity*	Date
....	....	....	....
....	....	....	....
....	....	....	....
....	....	....	....
....	....	....	....
....	....	....	....

E. P. 4-21 * See note below.

* *Note.*—The application and verification are to be signed—

(a) in the case of an individual, by the individual himself;

(b) in the case of an individual who is dead, by the person, who, under a letter of administration, probate or succession certificate, is entitled to the refund;

(c) in the case of a Company, local authority, or any other public body, by the principal officer, as defined in sub-section (12) of Section 2 of the Indian Income-tax Act, 1922;

(d) in the case of a Company which is in the course of winding up, by the liquidator of the Company;

(e) in the case of a Hindu Undivided Family, by the Manager or *Karta*;

(f) in the case of a Hindu Undivided Family which is disrupted, by the person or persons to whom the deposit was assigned at the time of the disruption;

(g) in the case of a Firm, by any partner;

(h) in the case of a Firm which has ceased business, by all the partners constituting the firm during the relevant chargeable accounting period, with the substitution in the case of a deceased partner of the administrator or other legal representative."

Excess Profits Tax Establishment.

Notification No. 31 dated the 26th October, 1946.

In exercise of the powers conferred by sub section (3) of Section 3 of the Excess Profits Tax Act, 1940 (XV of 1940), as applied to the Central India Administered Areas, the Central Board of Revenue hereby directs that the following amendments shall be made in its notification No. 2-D/ Excess Profits Tax, dated the 13th January 1945, namely :—

In items 1 and 2 of column 1 of the Schedule annexed to the said notification, the words "United Provinces and" shall be deleted.

2. This amendment shall have effect from the 1st May 1946.

INCOME TAX ESTABLISHMENTS.

Notification under Section 5 (6).

Notification No. 31 dated 9th November, 1946.

In exercise of the powers conferred by sub-section (6) of Section 5 of the Indian Income-tax Act, 1922 (XI of 1922), and in supersession of its notification No. 19 Income-tax, dated the 1st April, 1939, the Central Board of Revenue appoints the officers specified in the 3rd, 4th, 5th and 6th columns of the Schedule annexed hereto, to perform all the functions of an Income-tax Officer, Inspecting Assistant Commissioner of Income-tax, Appellate Assistant Commissioner of Income-tax and the Commissioner of Income-tax respectively in respect of the persons specified in the corresponding entry in the 2nd column thereof.

Provided that nothing herein contained shall apply to cases or classes of cases assigned to a Commissioner of Income-tax appointed under sub-section (2) of Section 5 of the Indian Income-tax Act, 1922:—

SCHEDULE

Serial No.	Persons	Officer appointed to perform the functions of			
		Income-tax Officer	Inspecting Assistant Commissioner of Income-tax	Appellate Assistant Commissioner of Income-tax	Commissioner of Income-tax
1	2	3	4	5	6
1	Employees of the Madras and Southern Mahratta Railway except those under the audit of the Controller of Supply Accounts, Calcutta.	Income-tax Officer, Madras Salaries Circle.	Inspecting Assistant Commissioner of Income-tax, Central Range, Madras.	Appellate Assistant Commissioner of Income-tax, A Range, Madras.	Commissioner of Income-tax, Madras.
2	All Government servants under the audit of the Accountant General, Madras.	Income-tax Officer, Madras Salaries Circle.	Inspecting Assistant Commissioner of Income-tax, Central Range, Madras.	Appellate Assistant Commissioner of Income-tax, A Range, Madras.	Commissioner of Income-tax, Madras.
3	All Government servants who are under the audit of the Deputy Accountant General, Posts and Telegraphs, Madras, but do not reside in the Andaman Islands.	Income-tax Officer, Madras Salaries Circle.	Inspecting Assistant Commissioner of Income-tax, Central Range, Madras.	Appellate Assistant Commissioner of Income-tax, A Range, Madras.	Commissioner of Income-tax, Madras.
4	Indian employees in Sind, Punjab and Delhi of Messrs. Ralli Brothers.	Income-tax Officer, Salaries, Karachi.	Inspecting Assistant Commissioner of Income-tax, Karachi Range.	Appellate Assistant Commissioner of Income-tax, Karachi Range.	Commissioner of Income-tax, Sind and Baluchistan.
5	European staff of Messrs. Volkart Brothers working in the Punjab and Sind.	Income-tax Officer, Salaries, Karachi.	Inspecting Assistant Commissioner of Income-tax, Karachi Range.	Appellate Assistant Commissioner of Income-tax, Karachi Range.	Commissioner of Income-tax, Sind and Baluchistan.

1	2	3	4	5	6
6	Military employees formerly under the audit of the Controller of Military Accounts, Western Command, Karachi, but subsequently transferred to the audit control of the Controller of Military Accounts and Pensions, Lahore.	Income-tax Officer, Salaries, Quetta.	Inspecting Assistant Commissioner of Income-tax, Karachi Range	Appellate Assistant Commissioner of Income-tax, Karachi Range.	Commissioner of Income-tax, Sind and Baluchistan.
7	(i) Military employees under the audit control of the Controller of Military Accounts, Southern Command, Poona. (ii) Employees, whether civil or Military, who are members of, or are attached to, the Military Accounts Department and are under the audit control of the Field Controller of Military Accounts, Officers and Clearing House, Poona.	Income-tax Officer, Salaries and Poona District, Poona.	Inspecting Assistant Commissioner of Income-tax, Poona Range, Poona.	Additional Appellate Assistant Commissioner of Income tax, Belgaum Range, Poona.	Commissioner of Income-tax, Bombay Mofussil.
8	Persons (excluding those who fall under S. No. 70) not resident in British India and not assessed through statutory agents under Section 43 any part of whose income is derived from horse-racing	Income-tax Officer, Poona City.	Inspecting Assistant Commissioner of Income-tax, Poona Range, Poona.	Additional Appellate Assistant Commissioner of Income-tax, Belgaum Range, Poona.	Commissioner of Income-tax, Bombay Mofussil.
9	Persons (excluding those who fall under S. No. 70) not resident in British India whose total income is made up of income wholly taxed at source or dividends or both.	Income-tax Officer, Non-Residents' Refund Circle, Bombay.	Inspecting Assistant Commissioner of Income-tax, D Range, Bombay City.	Appellate Assistant Commissioner of Income-tax, D Range, Bombay City.	Commissioner of Income-tax, Bombay City.
10	Pensioners who draw their pensions in the United Kingdom and reside in Indian States.	Income-tax Officer, Non-Residents' Refund Circle, Bombay.	Inspecting Assistant Commissioner of Income-tax, D Range, Bombay City.	Appellate Assistant Commissioner of Income-tax, D Range, Bombay City.	Commissioner of Income-tax, Bombay City.
11	Pensioners who draw their pensions through Post Offices in Indian States and reside in those States.	Income-tax Officer, Non-Residents' Refund Circle, Bombay.	Inspecting Assistant Commissioner of Income-tax, D Range, Bombay City.	Appellate Assistant Commissioner of Income-tax, D Range, Bombay City.	Commissioner of Income-tax, Bombay City.
12	Religious and charitable institutions outside British India not liable to income-tax under Section 4 (3) (i) and (ii) of the Indian Income-tax Act, 1922, applying for refund of tax deducted at source on interest on securities or for exemption certificates in respect thereof.	Income-tax Officer, Non-Residents' Refund Circle, Bombay.	Inspecting Assistant Commissioner of Income-tax, D Range, Bombay City.	Appellate Assistant Commissioner of Income-tax, D Range, Bombay City.	Commissioner of Income-tax, Bombay City.
13	"Thana Funds" administered by Political Agents in Kathiawar.	Income-tax Officer, Non-Residents' Refund Circle, Bombay.	Inspecting Assistant Commissioner of Income-tax, D Range, Bombay City.	Appellate Assistant Commissioner of Income-tax, D Range, Bombay City.	Commissioner of Income-tax, Bombay City
14	Local or Thana Funds administered by Government officers in Indian States or in British administered areas in those States which are either not liable to income-tax or have been exempted under Section 60 of	Income-tax Officer, Non-Residents' Refund Circle, Bombay.	Inspecting Assistant Commissioner of Income-tax, D Range, Bombay City.	Appellate Assistant Commissioner of Income-tax, D Range, Bombay City.	Commissioner of Income-tax, Bombay City.

	the Act, when application is made on their behalf for refund of tax deducted at source on interest on securities or for exemption certificates in respect thereof.				
15	All persons assessed under Section 44C of the Act.	Income-tax Officer, Non-Residents' Refund Circle, Bombay.	Inspecting Assistant Commissioner of Income-tax, D Range, Bombay City.	Appellate Assistant Commissioner of Income-tax, D Range, Bombay City.	Commissioner of Income-tax, Bombay City.
16	Employees of the Bombay, Baroda and Central India Railway and the Great Indian Peninsula Railway except those under the audit of the Controller of Supply Accounts, Calcutta.	Income-tax Officer, Salaries, Section I, Bombay.	Inspecting Assistant Commissioner of Income-tax, E Range, Bombay City.	Appellate Assistant Commissioner of Income-tax, E Range, Bombay City.	Commissioner of Income-tax, Bombay City.
17	Government servants employed under the Director General of Observatories, Poona, the Directors, Madras and Kodaikanal Observatories, the Meteorologist Upper Air Observations, Agra, and the Meteorologist, Karachi, who are under the audit of the Accountant General, Bombay.	Income-tax Officer, Salaries, Section I, Bombay.	Inspecting Assistant Commissioner of Income-tax, E Range, Bombay City.	Appellate Assistant Commissioner of Income-tax, E Range, Bombay City.	Commissioner of Income-tax, Bombay City
18	Naval employees under the audit control of the Controller of Naval Accounts, Bombay.	Income-tax Officer, Salaries, Section I, Bombay.	Inspecting Assistant Commissioner of Income-tax, E Range, Bombay City.	Appellate Assistant Commissioner of Income-tax, E Range, Bombay City.	Commissioner of Income-tax, Bombay City.
19	Members of the Entertainments National Services Association serving in India.	Income-tax Officer, Salaries, Section I, Bombay.	Inspecting Assistant Commissioner of Income-tax, E Range, Bombay City.	Appellate Assistant Commissioner of Income-tax, E Range, Bombay City.	Commissioner of Income-tax, Bombay City.
20	Employees of the Rajputana Minerals Company, Limited.	Income-tax Officer, Salaries, Section II, Bombay.	Inspecting Assistant Commissioner of Income-tax, E Range, Bombay City.	Appellate Assistant Commissioner of Income-tax. E Range, Bombay City.	Commissioner of Income-tax, Bombay City.
21	Staff of Geologists and Geophysists under Burma Oil Company Limited, engaged in survey in Northern India having centres at Karachi and Digboi.	Income-tax Officer, Dibrugarh.	Inspecting Assistant Commissioner of Income-tax, Bengal, Range No. V and Assam.	Appellate Assistant Commissioner of Income-tax, Dacca Range.	Commissioner of Income-tax, Assam.
22	European employees in British India and Berar and Indian employees in Bengal, Bihar, Orissa, Assam and the United Provinces of Messrs. Ralli Brothers.	Income-tax Officer, Calcutta, District III-A.	Inspecting Assistant Commissioner of Income-tax, Range No. II, Calcutta.	Appellate Assistant Commissioner of Income-tax, Calcutta 'A' Range.	Commissioner of Income-tax, Calcutta.
23	European employees of the Imperial Tobacco Company (India) Limited and the Indian Leaf Tobacco Development Company Limited in the Provinces of Bombay, Madras, United Provinces, Punjab, Bengal, Bihar, Orissa and Assam.	Income-tax Officer, Calcutta, District III-A.	Inspecting Assistant Commissioner of Income-tax. Range No. II, Calcutta.	Appellate Assistant Commissioner of Income-tax, Calcutta 'A' Range.	Commissioner of Income-tax, Calcutta.

1	2	3	4	5	6
24	European employees of the Tobacco Manufacturers (India) Limited, and the Printers (India), Limited, in the Provinces of Bombay, Madras, United Provinces, Punjab, Bengal, Bihar, Orissa and Assam.	Income-tax Officer, Calcutta, District III-A.	Inspecting Assistant Commissioner of Income-tax, Range No. II, Calcutta.	Appellate Assistant Commissioner of Income-tax, Calcutta 'A' Range.	Commissioner of Income-tax, Calcutta.
25	Employees of the "Statesman Limited" stationed at Lahore and Delhi,	Income-tax Officer, Calcutta, District III-A.	Inspecting Assistant Commissioner of Income-tax, Range No. II, Calcutta.	Appellate Assistant Commissioner of Income-tax, Calcutta 'A' Range.	Commissioner of Income-tax, Calcutta.
26	Employees of Messrs. Burmah-Shell Oil Storage and Distributing Company of India, Limited, stationed at Delhi.	Income-tax Officer, Calcutta, District III-A.	Inspecting Assistant Commissioner of Income-tax, Range No. II, Calcutta.	Appellate Assistant Commissioner of Income-tax, Calcutta 'A' Range.	Commissioner of Income-tax, Calcutta.
27	Employees of the Bata Shoe Company Limited stationed anywhere in British India.	Income-tax Officer, Calcutta, District III-A.	Inspecting Assistant Commissioner of Income-tax, Range No. II, Calcutta.	Appellate Assistant Commissioner of Income-tax, Calcutta 'A' Range.	Commissioner of Income-tax, Calcutta.
28	All Government employees and pensioners under the audit of the Accountant General, Bengal, who are serving or residing in Bengal other than those who carry on business on their own account and those who are within the jurisdiction of the Income-tax Officer, Railways and Miscellaneous Salaries Circle, Calcutta.	Income-tax Officer, Central Salaries Circle, Calcutta.	Inspecting Assistant Commissioner of Income-tax, Range No. IV, Calcutta.	Appellate Assistant Commissioner of Income-tax, Calcutta 'A' Range.	Commissioner of Income-tax, Calcutta.
29	Pensioners, other than pensioners of the Central Government residing outside Bengal who are under the audit of the Accountant General, Bengal.	Income-tax Officer, Central Salaries Circle, Calcutta.	Inspecting Assistant Commissioner of Income-tax, Range No. IV, Calcutta.	Appellate Assistant Commissioner of Income-tax, Calcutta 'A' Range.	Commissioner of Income-tax, Calcutta.
30	(i) All Government employees and pensioners who were till 1920-21 under the audit of the Accountant General, Central Revenues, but are now under the audit of the Accountant General, Bengal, Calcutta; (ii) all military officers and pensioners whose salaries are audited by the Controller of Army Factory Accounts, Calcutta, (iii) all civil pensioners of the Central Government under the audit of the Accountant General, Bengal; and (iv) all Government officers serving in and pensioners from the offices of the Government Inspectors of Railways, Circles I & II, and in the offices of the Government Examiners of Accounts, Bengal and Assam Railway, East Indian Railway, and Bengal Nagpur Railway;	Income-tax Officer, Railways and Miscellaneous Salaries Circle, Calcutta.	Inspecting Assistant Commissioner of Income-tax, Range No. IV, Calcutta.	Appellate Assistant Commissioner of Income-tax, Calcutta 'A' Range.	Commissioner of Income-tax, Calcutta.

	who are serving or residing in Bengal other than those who carry on business on their own account.				
31	Employees of the Bengal Nagpur Railway.	Income-tax Officer, Railways and Miscellaneous Salaries Circle, Calcutta.	Inspecting Assistant Commissioner of Income-tax, Range No. IV, Calcutta.	Appellate Assistant Commissioner of Income-tax, Calcutta 'A' Range.	Commissioner of Income-tax, Calcutta.
32	Employees of the East Indian Railway.	Income-tax Officer; Railways and Miscellaneous Salaries Circie, Calcutta.	Inspecting Assistant Commissioner of Income-tax, Range No. IV, Calcutta.	Appellate Assistant Commissioner of Income-tax, Calcutta 'A' Range.	Commissioner of Income-tax, Calcutta.
33	Central Government servants serving outside Bengal and Central Government pensioners residing outside Bengal who are under the audit of the Accountant General, Bengal.	Income-tax Officer, Railways and Miscellaneous Salaries Circle, Calcutta.	Inspecting Assistant Commissioner of Income-tax, Range No. IV, Calcutta.	Appellate Assistant Commissioner of Income tax, Calcutta 'A' Range.	Commissioner of Income tax, Calcutta.
34	Employees under the audit of the Controller of Ordnance Factory Accounts and the Controller of Leather and Clothing Factory Accounts and all staff of the Factory Accounts Branch of the Military Accounts Department under the Chief Controller of Factory Accounts, Controller of Ordnance Factory Accounts, Controller of Leather and Clothing Factory Accounts and Controller of Accounts, Military Railway Claims	Income-tax Officer, Railways and Miscellaneous Salaries Circle, Calcutta.	Inspecting Assistant Commissioner of Income-tax, Range No. IV, Calcutta.	Appellate Assistant Commissioner of Income tax, Calcutta 'A' Range.	Commissioner of Income tax, Calcutta.
35	Pensioners whose pensions are payable from Defence Services Estimates through the Controller of Military Accounts and Pensions, Lahore, who reside in Bengal.	Income-tax Officer, Railways and Miscellaneous Salaries Circle, Calcutta.	Inspecting Assistant Commissioner of Income-tax, Range No. IV, Calcutta.	Appellate Assistant Commissioner of Income tax, Calcutta 'A' Range.	Commissioner of Income tax, Calcutta.
36	Employees of the Bengal and Assam Railway.	Income-tax Officer, Railways and Miscellaneous Salaries Circle, Calcutta.	Inspecting Assistant Commissioner of Income-tax, Range No. IV, Calcutta.	Appellate Assistant Commissioner of Income tax, Calcutta 'A' Range.	Commissioner of Income tax, Calcutta.
37	All employees and pensioners of the Posts and Telegraphs Department under the audit of the two Deputy Accountants General, Posts and Telegraphs (Postal and Telegraph Branches), Calcutta.	Income-tax Officer, Railways and Miscellaneous Salaries Circle, Calcutta.	Inspecting Assistant Commissioner of Income-tax, Range No. IV, Calcutta.	Appellate Assistant Commissioner of Income tax, Calcutta 'A' Range.	Commissioner of Income tax, Calcutta.
38	Employees of the India General Navigation and Railway Company Limited and River Steam Navigation Company Limited working in Bengal, Bihar, Orissa and Assam, except those who carry on business in addition.	Income-tax Officer, District V-A, Calcutta.	Inspecting Assistant Commissioner of Income-tax, Range No. II, Calcutta.	Appellate Assistant Commissioner of Income tax, Calcutta 'A' Range.	Commissioner of Income tax, Calcutta.

1	2	3	4	5	6
39	Employees of W. T. Henley's Telegraph Works Company Limited, stationed at Bombay, Karachi, Lahore, Delhi and Madras.	Income-tax Officer, District V-A, Calcutta.	Inspecting Assistant Commissioner of Income-tax, Range No. II, Calcutta.	Appellate Assistant Commissioner of Income tax, Calcutta 'A' Range.	Commissioner of Income tax, Calcutta.
40	Employees of the Oudh Tirhut Railway.	Income-tax Officer, Gorakhpur.	Inspecting Assistant Commissioner of Income-tax, Lucknow Charge.	Appellate Assistant Commissioner of Income tax, Benares Range.	Commissioner of Income tax, United Provinces and Ajmer-Merwara.
41	Employees of the Pertabpore Company Limited.	Income-tax Officer, Gorakhpur.	Inspecting Assistant Commissioner of Income-tax, Lucknow Charge.	Appellate Assistant Commissioner of Income tax, Benares Range,	Commissioner of Income tax, United Provinces and Ajmer-Merwara.
42	Persons under the audit of (i) the Chief Paymaster British Troops (India) Meerut, and (ii) the Controller of Military Accounts, Central Command, Meerut.	Income-tax Officer, Military Circle, Meerut.	Inspecting Assistant Commissioner of Income-tax, Meerut Charge.	Appellate Assistant Commissioner of Income tax, Agra Range.	Commissioner of Income tax, United Provinces and Ajmer-Merwara.
43	Government servants under the audit of the Deputy Accountant General, Posts and Telegraphs, Nagpur.	Income-tax Officer Salary Circle, Nagpur.	Inspecting Assistant Commissioner of Income-tax, Central Provinces and Berar.	Appellate Assistant Commissioner of Income tax, Central Provinces and Berar, Nagpur.	Commissioner of Income tax, Central Provinces and Berar.
44	Officers of the Women's Medical Service and of the Junior Branch of the same.	Income-tax Officer, Simla.	Inspecting Assistant Commissioner of Income-tax, Delhi.	Second Additional Appellate Assistant Commissioner of Income tax, Delhi Range, Ludhiana.	Commissioner of Income tax, Punjab, North West Frontier and Delhi Provinces.
45	Members of the Nursing Staff of the Lady Minto's Indian Nursing Association.	Income-tax Officer Simla.	Inspecting Assistant Commissioner of Income-tax, Delhi.	Second Additional Appellate Assistant Commissioner of Income tax, Delhi Range, Ludhiana.	Commissioner of Income tax, Punjab, North West Frontier and Delhi Provinces.
46	Government servants under the audit of the Accountant General, Central Revenues (excluding Government servants in the Indian Audit and Accounts Service attached to Railways and Postal Audit Offices), the Military Accountant General, the Deputy Accountant General, Posts and Telegraphs, Delhi Controller of Food Accounts or the Controller of Supply Accounts and Government servants residents in the Andamans who are subject to the audit of the Deputy Accountant General, Posts and Telegraphs, Madras.	Income-tax Officer, Salary Circle, Delhi.	Inspecting Assistant Commissioner of Income-tax, Delhi.	Appellate Assistant Commissioner of Income tax, Delhi.	Commissioner of Income tax, Punjab, North West Frontier and Delhi Provinces.
47	Persons (not being ex-enemy nationals) paid through the Controller, Local Clearing Office (Enemy Debts).	Income-tax Officer, Salary Circle, Delhi.	Inspecting Assistant Commissioner of Income-tax, Delhi.	Appellate Assistant Commissioner of Income tax, Delhi.	Commissioner of Income tax, Punjab, North West Frontier and Delhi Provinces.

48	Military pensioners resident in the States of Mewar, Bharatpur, Bikaner, Jaipur, Marwar, Alwar and Bhopal who are under the audit of the Controller of Military Accounts and Pensions, Lahore.	Income-tax Officer, Salary Circle, Delhi.	Inspecting Assistant Commissioner of Income-tax, Delhi.	Appellate Assistant Commissioner of Income-tax, Delhi.	Commissioner of Income-tax, Punjab, North West Frontier and Delhi Provinces.
49	Pensioners who draw their pensions from the Hyderabad (Deccan) Treasury, and are under the audit of the Accountant General, Central Revenues.	Income-tax Officer, Salary Circle, Delhi.	Inspecting Assistant Commissioner of Income-tax, Delhi.	Appellate Assistant Commissioner of Income-tax, Delhi.	Commissioner of Income-tax, Punjab, North West Frontier and Delhi Provinces.
50	Employees of the Eastern Group Supply Council and of the Central Provision Office.	Income-tax Officer, Salary Circle, Delhi.	Inspecting Assistant Commissioner of Income-tax, Delhi.	Appellate Assistant Commissioner of Income-tax, Delhi.	Commissioner of Income-tax, Punjab, North West Frontier and Delhi Provinces.
51	(i) Persons under the audit control of the Controller of Accounts, Air Forces, Dehra-Dun.	Income-tax Officer, Ambala.	Inspecting Assistant Commissioner of Income-tax, Delhi.	Second Additional Appellate Assistant Commissioner of Income-tax, Delhi Range, Ludhiana.	Commissioner of Income-tax, Punjab, North West Frontier and Delhi Provinces.
	(ii) All employees, whether civil or military, who are members of or are attached to the Military Accounts Department and are under the audit control of the Field Controller of Military Accounts, other Ranks, Ambala.	Income-tax Officer, Ambala.	Inspecting Assistant Commissioner of Income-tax, Delhi.	Second Additional Appellate Assistant Commissioner of Income-tax, Delhi Range, Ludhiana.	Commissioner of Income-tax, Punjab, North West Frontier and Delhi Provinces.
52	(i) Military employees under the audit control of the Controller of Military Accounts, Northern Command, Rawalpindi.	Income-tax Officer, Military Circle, Rawalpindi.	Inspecting Assistant Commissioner of Income-tax, Lahore Division, Lahore.	Appellate Assistant Commissioner of Income-tax, Rawalpindi Range, Rawalpindi.	Commissioner of Income-tax, Punjab, North West Frontier and Delhi Provinces, Lahore.
	(ii) Military employees, excluding those who are covered by any one of the other items in this Schedule, who are under the audit control of the Controller of Military Accounts and Pensions, Lahore.	Income-tax Officer, Military Circle, Rawalpindi.	Inspecting Assistant Commissioner of Income-tax, Lahore Division, Lahore.	Appellate Assistant Commissioner of Income-tax, Rawalpindi Range, Rawalpindi.	Commissioner of Income-tax, Punjab, North West Frontier and Delhi Provinces, Lahore.
53	Employees of the North Western Railway except those under the audit of the Controller of Supply Accounts, Calcutta.	Income-tax Officer, Salary Circle, Lahore.	Inspecting Assistant Commissioner of Income-tax, Lahore Division.	Appellate Assistant Commissioner of Income-tax, Lahore.	Commissioner of Income-tax, Punjab, North West Frontier and Delhi Provinces, Lahore.
54	Employees of the Church Missionary Society, Church of England Zenana Missionary Society, and Church and Mission of Central Council of the Church Missionary Society residing in the Punjab, North West Frontier Provinces, Sind and Baluchistan.	Income-tax Officer, D—Ward, Lahore.	Inspecting Assistant Commissioner of Income-tax, Lahore Division.	Appellate Assistant Commissioner of Income-tax, Lahore.	Commissioner of Income-tax, Punjab, North West Frontier and Delhi Provinces, Lahore.
55	Employees of the American United Presbyterian Mission residing in the United	Income-tax Officer, Gujranwala.	Inspecting Assistant Commissioner of Income-tax, Lahore Division.	Appellate Assistant Commissioner of Income-tax, Lahore.	Commissioner of Income-tax, Punjab,North-

1	2	3	4	5	6
	Provinces, in the Punjab and the North West Frontier Province.				West Frontier and Delhi Provinces, Lahore.
56	Government Employees under the audit control of the Accountant General, Punjab, residing in Indian States.	Income-tax Officer, Salary Circle, Lahore.	Inspecting Assistant Commissioner of Income-tax, Lahore Division.	Appellate Assistant Commissioner of Income-tax, Lahore.	Commissioner of Income-tax, Punjab, North West Frontier and Delhi Provinces, Lahore.
57	All Civil Gazetted employees of the Government of Burma under the audit of the Accountant General, Burma, and all Gazetted and non-Gazetted employees of the Posts and Telegraphs Department, Burma, under the audit of the Controller of Posts and Telegraphs Accounts, Burma.	Income-tax Officer, Simla.	Inspecting Assistant Commissioner of Income-tax, Delhi.	Second Additional Appellate Assistant Commissioner of Income-tax, Delhi Range, Ludhiana.	Commissioner of Income-tax, Punjab, North West Frontier and Delhi Provinces, Lahore.
58	Employees of the Government of Burma, excluding those who fall under Serial No. 57, and all Burma evacuees at Simla, excluding those who are covered by any of the other items in this Schedule.	Additional Income-tax Officer, Simla.	Inspecting Assistant Commissioner of Income-tax, Delhi.	Second Additional Appellate Assistant Commissioner of Income-tax, Delhi Range, Ludhiana.	Commissioner of Income-tax, Punjab, North West Frontier and Delhi Provinces, Lahore.
59	Government servants under the audit of the Accountant General, Bihar excluding persons any part of whose income is derived from the exercise of a profession.	Income-tax Officer, Salaries Circle, Ranchi.	Inspecting Assistant Commissioner of Income-tax, Northern Range, Patna.	Appellate Assistant Commissioner of Income-tax. in their respective Ranges.	Commissioner of Income-tax, Bihar and Orissa.
60	Government pensioners under the audit of the Accountant General, Bihar, excluding persons any part of whose income is derived from the exercise of a profession.	Income-tax Officer, Salaries Circle, Ranchi.	Inspecting Assistant Commissioner of Income-tax, Northern Range, Patna.	Appellate Assistant Commissioner of Income-tax, in their respective Ranges.	Commissioner of Income-tax, Bihar and Orissa.
61	Employees of the Tin Plate Company of India Limited, Golmuri (near Jamshedpur) excluding persons any part of whose income is derived from the exercise of a profession.	Income-tax Officer, Salaries Circle, Ranchi.	Inspecting Assistant Commissioner of Income-tax, Northern Range, Patna.	Appellate Assistant Commissioner of Income-tax, in their respective Ranges.	Commissioner of Income-tax, Bihar and Orissa.
62	Employees of the Tata Iron Steel Company at Jamshedpur excluding persons any part of whose income is derived from the exercise of a profession.	Income-tax Officer, Salaries Circle, Ranchi.	Inspecting Assistant Commissioner of Income-tax, Northern Range, Patna.	Appellate Assistant Commissioner of Income-tax, in their respective Ranges.	Commissioner of Income-tax, Bihar and Orissa.
63	Employees of the European Mental Hospital, Ranchi, excluding persons any part of whose income is derived from the exercise of a profession.	Income-tax Officer, Salaries Circle, Ranchi.	Inspecting Assistant Commissioner of Income-tax, Northern Range, Patna.	Appellate Assistant Commissioner of Income-tax, in their respective Ranges.	Commissioner of Income-tax, Bihar and Orissa.
64	Employees of the Indian Mental Hospital, Ranchi, excluding persons any part of whose income is derived from the exercise of a profession.	Income-tax Officer, Salaries Circle, Ranchi.	Inspecting Assistant Commissioner of Income-tax, Northern Range, Patna.	Appellate Assistant Commissiouer of Income-tax, in their respective Ranges.	Commissioner of Income-tax, Bihar and Orissa.
65	Employees of the Lac Research Institute, Namkum (near Ranchi) excluding persons	Income-tax Officer, Salaries Circle, Ranchi.	Inspecting Assistant Commissioner of Income-tax, Northern Range, Patna.	Appellate Assistant Commissioner of Income-tax, in their respective Ranges.	Commissioner of Income-tax, Bihar and Orissa.

	any part of whose income is derived from the exercise of a profession.				
66	Government servants and pensioners under the audit of the Comptroller, Orissa, excluding persons any part of whose income is derived from the exercise of a profession.	Income-tax Officer, Salaries Circle, Ranchi.	Inspecting Assistant Commissioner of Income-tax, Northern Range, Patna.	Appellate Assistant Commissioner of Income-tax, in their respective Ranges.	Commissioner of Income tax, Bihar and Orissa.
67	Personnel paid from the Defence Services Estimates who are in the payment of the Controller of Military Accounts, Eastern Command, Patna.	Income-tax Officer, Patna.	Inspecting Assistant Commissioner of Income-tax, Northern Range, Patna.	Appellate Assistant Commissioner of Income-tax, Patna.	Commissioner of Income tax, Bihar and Orissa.
68	Persons not resident in British India assessed through statutory agents under Section 43 of the Indian Income-tax Act, 1922, whether their income arises in a single province or in more than one province.	Income-tax Officer of the district in which the statutory agent carries on the business by reason of which income tax is chargeable in his name under Section 42 or where he resides, as the case may be.	Inspecting Assistant Commissioner of Income-tax who has been appointed to perform the function of an Inspecting Assistant Commissioner in the area where the Income-tax Officer referred to in column 3 has jurisdiction.	Appellate Assistant Commissioner of Income-tax who has been invested with powers to hear appeals against the decision of the Income-tax Officer referred to in column 3.	Commissioner of Income tax of the Province concerned.
69	Persons (excluding those who fall under S. No. 70) not resident in British India who do not fall under serial Nos. 8 and 9 and not assessed through statutory agents under Section 43 with any income for direct assessment, *e.g.*, house property, interest, etc.	The Income-tax Officer, of the Circle in which arose the greater part of the income for assessment in 1939-40, or in the first year of assessment, whichever year is later; Provided that the same officer shall have jurisdiction for subsequent years so long as some income for direct assessment (not necessarily the greater part) continues to arise within his jurisdiction.	Inspecting Assistant Commissioner of Income-tax who has been appointed to perform the functions of an Inspecting Assistant Commissioner of Income-tax in the area where the Income-tax Officer referred to in column 3 has jurisdiction.	Appellate Assistant Commissioner of Income-tax who has been invested with powers to hear appeals against the decision of the Income-tax Officer referred to in column 3.	Commissioner of Income tax of the Province concerned.
70	(*i*) Defence Services Employees under the audit control of the Field Controller of Military Accounts, Officers and Clearing House, Poona, and/or the Field Controller of Military Accounts other Ranks, Ambala, excluding (*a*) Employees, whether civil or military, who are members of or are attached to the Military Accounts Department, and (*b*) Employees who are partners in a firm in British India or who have income from business carried on in British India. (*ii*) Persons resident outside India who at the time of departure from India were	Income-tax Officer attached to the Adjutant General's Branch, General Headquarters India and stationed at Poona.	Inspecting Assistant Commissioner of Income-tax, Poona Range, Poona.	Additional Appellate Assistant Commissioner of Income-tax, Belgaum Range, Poona.	Commissioner of Income tax, Bombay Mofussil.

1	2	3	4	5	6
	Defence Services employees under the audit control of the Field Controller of Military Accounts, Officers and Clearing House, Poona (or previously Field Controller of Military Accounts, Poona) or the Field Controller of Military Accounts, other Ranks, Ambala and who are *not* under the audit control of any other Audit Officer in India in respect of accounting periods during which they were Defence Services employees in Indian Payment. (iii) Persons being widows or dependents of Defence Service employees, in the payment of the Field Controller of Military Accounts, Officers and Clearing House, Poona (or previously Field Controller of Military Accounts, Poona) or the Field Controller of Military Accounts, Other Ranks, Ambala.				
71	Persons in the payment of Force 136, Dholpur House, New Delhi.	Income-tax Officer attached to the Adjutant General's Branch, General Headquarters, India and stationed at Poona.	Inspecting Assistant Commissioner of Income-tax, Poona Range, Poona.	Additional Appellate Assistant Commissioner of Income-tax, Belgaum Range, Poona.	Commissioner of income-tax, Bombay Mofussil.
72	Air Forces employees whose accounts are maintained by the Base Accounts Office, Air Forces, Bombay and the Indian Air Force Central Accounts Office, Bombay, and the employees of the office of the Base Auditor, Royal Air Force, Bombay.	Income tax Officer, Air Forces, Bombay.	Inspecting Assistant Commissioner of Income tax, B-Range, Bombay.	Appellate Assistant Commissioner of Income tax, B-Range, Bombay.	Commissioner of Income tax, Bombay City.

Notification No. 32 dated the 9th November, 1946.

In pursuance of sub-section (4) of Section 5 of the Indian Income-tax Act, 1922 (XI of 1922), and in supersession of its notification No. 58-Income-tax, dated the 15th July 1939, the Central Board of Revenue directs—

(i) that the Appellate Assistant Commissioners of Income-tax of the Ranges specified in column 1 of the Schedule hereto annexed shall perform their functions in respect of all persons and incomes assessed to income-tax, or supertax in the Income-tax Circles and wards specified in the corresponding entry in column 2 thereof, and

(ii) that the Appellate Assistant Commissioner of Income-tax of Bombay "D" Range shall also perform his functions in respect of persons appealing from orders of the Income-tax Officers of the Non-Residents Refund Circle.

SCHEDULE.

Range.	Income-tax Circles and Wards.
I. *Madras*	
Bezwada.	(1) Vizianagaram.
	(2) Vizagapatam.
	(3) Cocanada.
	(4) Rajahmundry.
	(5) Ellore.
	(6) Masulipatam.
	(7) Bezwada I.
	(8) Bezwada II.
	(9) Guntur.
	(10) Tenali.
	(11) Bapatla.
	(12) Kurnool.
	(13) Bellary.
Madras "A"	(1) Madras II.
	(2) Madras V.
	(3) Madras VI.
	(4) Salem I.
	(5) Salem II.
	(6) Madras (Special) Central.
	(7) Madras (Special) South.
	(8) Nellore I.
	(9) Nellore II.
Madras "B"	(1) Madras I.
	(2) Madras III.
	(3) Madras IV.
	(4) Conjeevaram.
	(5) Cuddalore.
	(6) Vellore.
	(7) Chittoor.
	(8) Cuddappah.
	(9) Anantapur.
	(10) Madras (Special) North.
	(11) Madras (Special) East.
Coimbatore.	(1) Coimbatore I.
	(2) Coimbatore II.
	(3) Coimbatore (Special).
	(4) Ootacamund.
	(5) Palghat.
	(6) Calicut.
	(7) Mangalore.
	(8) Coorg.
Trichinopoly.	(1) Trichinopoly I.
	(2) Trichinopoly II.
	(3) Negapatam.
	(4) Tanjore.
	(5) Dindigul.
	(6) Madura (North).
	(7) Madura (South).
	(8) Karaikudi I.
	(9) Karaikudi II.
	(10) Virudhunagar.
	(11) Tinnevelly.
	(12) Tuticorin.
	(13) Madura (Special).
	(14) Erode.
	(15) Erode (Special).
II. *Bombay City*	
Bombay "A"	(1) A-I ward.
	(2) A-II ward.
	(3) A-III ward.
	(4) A-IV ward.
	(5) A-V ward.
	(6) G ward.
	(7) M ward.
	(8) D-I ward.
	(9) D-II ward.
Bombay "B"	(1) Companies Circle I.
	(2) Companies Circle II.
	(3) Companies Circle III.
	(4) Companies Circle IV.
	(5) Air Force Circle, Bombay.
Bombay "C"	(1) B-I ward.
	(2) B-II ward.
	(3) B-III ward.
	(4) C-I ward.
	(5) C-II ward.
	(6) C-III ward.
	(7) C-IV ward.
Bombay "D"	(1) Central Section I.
	(2) Central Section II.
	(3) Central Section III.
	(4) Central Section IV.

Range.	Income-tax Circles and Wards.
Bombay "D"— (contd.)	(5) Central Section V.
	(6) Central Section VI.
	(7) Central Section VII.
	(8) Central Section VIII.
	(9) Central Section IX.
	(10) Central Section X.
	(11) Central Section XI.
	(12) Central Section XII.
	(13) E. Ward.
Bombay "E"	(1) Bombay Circle I.
	(2) Bombay Circle II.
	(3) Bombay Circle III.
	(4) Bombay Circle IV.
	(5) Bombay Circle V.
	(6) Bombay Circle VI.
	(7) Bombay Circle VII.
	(8) Bombay Circle VIII.
	(9) Bombay Circle IX.
	(10) Bombay Circle X.
	(11) Bombay Circle XI.
	(12) Bombay Circle XII.
	(13) Bombay Circle XIII.
	(14) Bombay Circle XIV.
	(15) Bombay Circle XV.
	(16) Bombay Circle XVI.
	(17) Bombay Suburban District.
	(18) Salaries Section I.
	(19) Salaries Section II.
	(20) Bombay Refund Circle.

III. *Bombay Mofussil.*

Range.	Income-tax Circles and Wards.
Ahmedabad.	(1) Ahmedabad City and District.
	(2) Ahmedabad.
	(3) Kaira District.
	(4) Broach and Panch Mahals District.
	(5) Surat City and District.
Belgaum.	(1) Ahmednagar District.
	(2) Satara District.
	(3) Sholapur District.
	(4) Belgaum and Kanara below Ghat Talukas.
	(5) Dharwar and Kanara above Ghat Talukas
	(6) Bijapore District.
	(7) Kolaba and Ratnagiri District.
	(8) Poona City.
	(9) Poona District and Salariess.
	(10) Nasik District.
	(11) East Khandesh District.
	(12) West Khandesh District.
	(13) Thana District.

IV. *Sind and Baluchistan.*

Range.	Income-tax Circles and Wards.
Karachi.	(1) Karachi City and Taluka.
	(2) Hyderabad District.
	(3) Sukkur and Nawabshah Districts.
	(4) Shikarpur and Upper Sind Frontier District.
	(5) Larkana and Dadu District.
	(6) Karachi and Thar Parkar District (excluding Karachi Taluka).
	(7) British Baluchistan.
	(8) Karachi.

V. *Calcutta, Bengal Mofussil and Assam.*

Range.	Income-tax Circles and Wards.
Calcutta 'A'.	(1) Calcutta District I (1).
	(2) Calcutta District I (2)
	(3) Calcutta District II (1).
	(4) Calcutta District II (2).
	(5) Calcutta District III (1).
	(6) Calcutta District III (2).
	(7) Calcutta District III-A.
	(8) Calcutta District IV (1).
	(9) Calcutta District IV (2).
	(10) Calcutta District IV (3).
	(11) Calcutta District V.
	(12) Calcutta District V-A.
	(13) Calcutta District VI.
	(14) Companies Circle I Calcutta.
	(15) Companies Circle II Calcutta.
	(16) Companies Circle III Calcutta
	(17) Companies Circle IV Calcutta.
	(18) Non-companies Excess Profits Tax Circle, Calcutta.
	(19) Central Salaries Circle, Calcutta.
	(20) Railways and Miscellaneous Salaries Circle, Calcutta.
	(21) Central Income-tax Circle I to VI.
Calcutta 'B'.	(1) 24 Parganas.
	(2) Howrah.
	(3) Khulna-Jessore.
	(4) Midnapur-Bankura.
	(5) Burdwan-Birbhum.
	(6) Murshidabad-Nadia.
	(7) Hooghly.
	(8) Jalpaiguri-Darjeeling.
	(9) Dinajpur-Maldah.
	(10) Rangpur-Bogra.
	(11) Rajshahi-Pabna.
	(12) Central Income-tax Circle III Additional.
Dacca.	(1) Dibrugarh sub-division of Lakhimpur District and the Sodiya Frontier Tract.
	(2) Sibsagar and Naga Hill Districts Manipur and North Lakhimpur sub-division of the Lakhimpur District.
	(3) Nowgong Darang and Balipara Frontier Tract.
	(4) Cachar and Lushai Hills Districts and Karimganj sub-divisions of Sylhet District.
	(5) Kamrup, Goalpara Garo Hills.
	(6) North Sylhet, South Sylhet, Habiganj and Sunamganj sub-division of Sylhet District and Khasi and Jaintia Hills District.
	(7) Dacca.
	(8) Bakarganj.
	(9) Faridpur.
	(10) Tipperah-Noakhali.
	(11) Mymensing.
	(12) Chittagong.

VI—*United Provinces and Ajmer-Merwara.*

Range.	Income-tax Circles and Wards.
Cawnpore.	(1) Cawnpore. (2) Special Income-tax cum Excess Profits Tax Circle, Cawnpore. (3) Fatehgarh.
Lucknow.	(1) Lucknow. (2) Sitapur. (3) Bareilly. (4) Gonda. (5) Fyzabad. (6) Allahabad. (7) Central Circle, Allahabad.
Meerut.	(1) Meerut. (2) Military Circle, Meerut. (3) Saharanpur. (4) Dehradun. (5) Moradabad.
Agra.	(1) Agra. (2) Aligarh. (3) Jhansi. (4) Ajmer-Merwara.
Benares.	(1) Benares (2) Azamgarh. (3) Gorakhpur.

VII—*Central Provinces and Berar.*

Range.	Income-tax Circles and Wards.
Nagpur.	(1) Income-tax cum Excess Profits Tax Circle, Nagpur. (2) Akola. (3) Khamgaon. (4) Nagpur. (5) Wardha. (6) Yeotmal. (7) Amraoti. (8) Salary Circle, Nagpur.
Jabbulpore.	(1) Jabbulpore. (2) Saugor. (3) Chindwara. (4) Raipur. (5) Khandwa.

VIII—*Punjab, North-west Frontier Province and Delhi.*

Range.	Income-tax Circles and Wards
Lahore.	(1) Lahore. (2) Salaries Circle, Lahore. (3) Lyallpur. (4) Gujranwala. (5) Gujrat. (6) Sargodha. (7) Montgomery. (8) Multan. (9) Jhelum.
Rawalpindi.	(1) Rawalpindi. (2) Peshawar. (3) Nowshera. (4) Dehra Ismail Khan.
Amritsar.	(1) Amritsar. (2) Jullundur. (3) Gurdaspur. (4) Sialkot. (5) Hoshiarpur.
Delhi.	(1) Delhi. (2) Salary Circle, Delhi. (3) Hissar. (4) Rohtak. (5) Ambala. (6) Simla. (7) Ludhiana. (8) Ferozpur, (9) Karnal.

IX—*Bihar and Orissa.*

Range.	Income-tax Circles and Wards
Patna.	(1) Patna. (2) Bhagalpur. (3) Special Circle, Patna. (4) Special Circle. Cuttack. (5) Gaya. (6) Shahabad Palamau Circle, Arrah. (7) Sonthal Parganas. (8) Hazaribagh. (9) Purnea.
Purulia.	(1) Ranchi-Manbhum Sadar. (2) Singhbhum-Sambalpur. (3) Cuttack-Balasore. (4) Ganjam Puri Koraput. (5) Dhanbad.
Muzaffarpur.	(1) Muzaffarpur. (2) Saran. (3) Champaran. (4) Darbhanga. (5) Monghyr.

Notification No. 33 dated the 9th November, 1946.

In exercise of the powers conferred by sub-section (6) of Section 5 of the Indian Income-tax Act, 1922 (XI of 1922), as applied to the Hyderabad Administered Areas and in supersession of its notification No. 2-D., dated the 2nd March 1940, the Central Board of Revenue appoints the officers specified in the 3rd, 4th, 5th and 6th columns of the Schedule annexed hereto, to perform all the functions of an Income-tax Officer, Inspecting Assistant Commissioner of Income-tax, Appellate Assistant Commissioner of Income-tax and the Commissioner of Income-tax respectively, in respect of the persons specified in the corresponding entry in the 2nd column thereof.

SCHEDULE

Serial No.	Persons	Officers to be appointed to perform the function of			
		Income-tax Officer	Inspecting Assistant Commissioner of Income-tax	Appellate Assistant Commissioner of Income-tax	Commissioner of Income-tax
1	2	3	4	5	6
1	All Government servants who are under the audit of the Deputy Accountant General, Posts and Telegraphs, Madras.	Income tax Officer, Madras Salaries Circle.	Inspecting Assistant Commissioner of Income tax, Central Range, Madras	Appellate Assistant Commissioner of Income tax, A' Range, Madras.	Commissioner of Income tax, Madras.
2	Military employees under the audit control of the Controller of Military Accounts, Southern Command, Poona.	Income tax Officer, Salaries and Poona District, Poona.	Inspecting Assistant Commissioner of Income tax, Poona Range, Poona.	Additional Appellate Assistant Commissioner of Income tax, Belgaum Range, Poona.	Commissioner of Income tax, Bombay Mofussil.
3	Employees of the Great Indian Peninsula Railway.	Income tax Officer, Salaries Section I, Bombay.	Inspecting Assistant Commissioner of Income tax, "E" Range, Bombay City.	Appellate Assistant Commissioner of Income tax, "E" Range, Bombay City.	Commissioner of Income tax Bombay City.
4	All employees and pensioners of the Posts and Telegraphs Department under the audit of the two Deputy Accountants General, Posts and Telegraphs (Postal and Telegraphs Branches) Calcutta.	Income tax Officer, Railways and Miscellaneous Salaries Circle, Calcutta.	Inspecting Assistant Commissioner of Income tax, Range No. IV, Calcutta.	Appellate Assistant Commissioner of Income tax, Calcutta 'A' Range.	Commissioner of Income tax, Calcutta.
5	Government servants and British subjects in the Service of a local authority established in exercise of the powers of the Crown Representative in that behalf who are under the audit of the Accountant General, Central Revenues.	Income tax Officer, Salary Circle, Delhi.	Inspecting Assistant Commissioner of Income tax, Delhi.	Appellate Assistant Commissioner of Income tax, Delhi Range.	Commissioner of Income tax, Punjab, North West Frontier and Delhi Provinces.
6	Pensioners who draw their pensions from the Hyderabad (Deccan) Treasury and are under the audit of the Accountant General, Central Revenues.	Income tax Officer, Salary Circle, Delhi.	Inspecting Assistant Commissioner of Income tax, Delhi.	Appellate Assistant Commissioner of Income tax, Delhi Range.	Commissioner of Income tax, Punjab, North West Frontier and Delhi Provinces.

Notification No. 34 dated 23rd November, 1946.

A list of associations, universities, colleges and institutions approved by the prescribed authority for the purpose of clause (xiii) of sub-section (2) of Section 10 of the Indian Income-tax Act, 1922 (XI of 1922), is published for general information.

LIST.

Agricultural Research Associations.

1. All India Bee Keepers' Association, Ramgarh, District, Nainital, U. P.
2. Botanical Survey of India, Calcutta.
3. Bombay Natural History Society, Bombay.
4. Central Board of Irrigation, Simla.
5. Current Science Association, Bangalore.
6. Entomological Society of India, Cawnpore.
7. Geological Survey of India, Dehra Dun.
8. Imperial Chemical Industries, Calcutta.
9. Imperial Council of Agricultural Research, New Delhi.
10. Indian Academy of Science, Bangalore.
11. Indian Botanical Society, Government College, Lahore.
12. Indian Central Cotton Committee, Bombay.
13. Indian Central Coconut Committee, Ernakulam.
14. Indian Central Jute Committee, Calcutta.
15. Indian Central Oilseeds Committee.
16. Indian Central Sugarcane Committee, New Delhi.
17. Indian Central Tobacco Committee, Bombay.
18. Indian Coffee Board, Bangalore.
19. Indian Chemical Society, Calcutta.
20. Indian Lac Cess Committee, Ranchi.
21. Indian Rubber Production Board, Kottayam, Travancore State.
22. Indian Science News Association, Calcutta.
23. Indian Society of Genetics Plant Breeding, New Delhi.
24. Indian Society of Soil Science, Calcutta.
25. Indian Tea Association, Calcutta.
26. Indian Tea Market Expansion Board, Calcutta.
27. Meteorological Department, Poona.
28. National Academy of Science, Allahabad.
29. Punjab Board of Economic Enquiry, Lahore.
30. Royal Asiatic Society, Calcutta & Bombay.
31. United Planters' Association of South India, Coonoor.
32. Vivekanand Laboratories, Almora.
33. Zoological Survey of India, Calcutta.

Scientific and Industrial Research Associations.

1. B. B. & C. I. Railway Workshop, Ajmer.
2. Bengal Potteries Ltd., Calcutta.
3. Bhowmik (Mr. B.B.), Radan House 89, Kalighat Road, Calcutta.
4. Biochemical Standardisation, Laboratory, Calcutta.
5. Botanical Survey of India, Calcutta.
6. Council of Scientific & Industrial Research, New Delhi.
7. Indian Central Cotton Committee, Matunga, Bombay.
8. Indian Crucible Co., Ltd., 16, Sibogopal Banerjee Lane, Salikia, Howrah.
9. Indian Meteorological Department, Delhi.
10. Mysore Iron & Steel Works, Bhadravati.
11. Provincial Broadcasting Department, Madras.
12. Royal Botanical Gardens, Calcutta.
13. Tata Iron & Steel Industry, Jamshedpur.

Associations connected with Research work in Medicine.

1. Enquiries conducted under the auspices of the I.R.F.A., New Delhi.
2. Indian Research Fund Association, New Delhi.
3. Medical Council of India, New Delhi.
4. Nutrition Research Laboratories, Coonoor.
5. Parlakimedi Trust Fund, New Delhi.
6. Tuberculosis Association of India, New Delhi.

UNIVERSITIES.

1. Agra University, Agra.
2. Allahabad University, Allahabad.
3. Andhra University, Guntur.
4. Annamalai University, Annamalainagar.
5. Bombay University (Chemical Technological Department), Bombay.
6. Calcutta University, (University College of Science), Calcutta.
7. Dacca University, Dacca.
8. Delhi University, Delhi.
9. Hindu University, Benares.
10. Lucknow University, Lucknow.
11. Madras University, Madras.
12. Muslim University, Aligarh.
13. Mysore University, Bangalore.
14. Nagpur University, Nagpur.
15. Patna University, Patna.
16. Punjab University, Lahore.
17. Travancore University, Trivandrum.
18. Usmania University, Hyderabad (Deccan).
19. Utkal University, Cuttack.
20. Women's University, Bombay.

COLLEGES.

1. Agricultural College, Cawnpore.
2. Agricultural College, Lyallpur.
3. Agricultural College, Nagpur.
4. Agricultural College, Poona.

5. Agricultural College, Sabour, Bihar.
6. Agricultural College, Saidapet.
7. Agricultural College, Sakrand, Sind.
8. Amar Singh K. E. M. U. Jat College, Lakhaoti, U. P.
9. Balwant Agricultural College, Agra.
10. Forman Christian College, Lahore.
11. Government College, Lahore.
12. Indian School of Mines, Dhanbad.
13. Islamia College, Peshawar.
14. Khalsa College, Amritsar.
15. King George's Medical College, Lucknow.
16. Presidency College, Calcutta.
17. Presidency College, Madras.
18. Recognised Medical Colleges.
19. Science College, Patna.
20. Tropical School of Medicine, Calcutta.
21. Veterinary College, Bengal.
22. Veterinary College, Lahore.
23. Veterinary College, Madras.
24. Veterinary College, Patna.
25. Veterinary College, Poona.

INSTITUTIONS.

1. Agricultural Research Institute & College, Coimbatore.
2. Allahabad Agricultural Institute, Allahabad.
3. Bengal Agricultural Research Institute, Dacca.
4. Bengal Tanning Institute, Calcutta.
5. Bose Research Institute, Calcutta.
6. Central Irrigation Research Institute, Poona.
7. Central Research Institute, Trivandrum.
8. Forest Research Institute & College, Dehra Dun.
9. Government Silk Institute, Nathnagar, Bhagalpore.
10. Imperial Agricultural Research Institute, New Delhi.
11. Imperial Dairy Research Institute, Bangalore.
12. Imperial Veterinary Research Institute, Muktesar Izatnagar, U. P.
13. Imperial Institute of Sugar Technology, Cawnpore.
14. Indian Institute of Fruit Technology, Lyallpur.
15. Indian Institute of Science, Bangalore.
16. Indian Statistical Institute, Calcutta.
17. Institute of Agriculture, Anand.
18. Institute of Plant & Industry, Indore.
19. Irrigation Research Institute, Lahore.
20. Laxmi-Narain Institute of Technology, Nagpur.
21. National Institute of Science in India, Calcutta.
22. Nutritional Research Institute, Coonoor.
23. River Research Institute, Bengal, Calcutta.
24. Royal Institute of Science, Bombay.
25. Silk Research Institute, Berhampore.
26. Tata Institute of Fundamental Research, Bombay.
27. Technological Institute, Baroda.
28. Victoria Jubilee Technical Institute, Bombay.
29. Vishvabharti Institute, Calcutta.

Notification No. 24-D dated the 23rd November 1946.

In exercise of the powers conferred by sub-section (3) of Section 5 of the Indian Income-tax Act, 1922 (XI of 1922), the Central Government is pleased to cancel the notification of the Finance Department (Central Revenues), No. 39 Income-tax, dated the 29th July, 1939.

THE
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VOLUME XIV
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[IN THE ALLAHABAD HIGH COURT.]

RAM LAL BECHAIRAM *v.* COMMISSIONER OF INCOME-TAX.

BRAUND and MALIK, JJ.

March 7, 1945.

INDIAN INCOME-TAX ACT (XI OF 1922 BEFORE IT WAS AMENDED IN 1939), SEC. 4 (1) & (2)—SALE OF GOODS—RECEIPT OF INCOME—GOODS SENT TO BRITISH INDIAN HEAD OFFICE BY FOREIGN BRANCH—INVOICE PRICE INCLUDING PROFIT OF BRANCH—SALE IN BRITISH INDIA—WHERE PROFITS ACCRUE—CALCULATION OF PROFIT—ASSESSMENT AS REMITTED PROFIT—LEGALITY—PRESUMPTION.

The assessee, a trading Hindu undivided family resident in British India, had its head office in British India and a branch outside British India. Goods invoiced at Rs. 65,203 were sent from the branch to the head office. The invoice price included a profit margin equal to the profit that the branch would have derived if it had sold the goods to the head office. The head office remitted to the branch Rs. 59,175 leaving a credit balance of Rs. 6,028 in its books in favour of the branch. The Income-tax Officer estimated the profit of the branch at Rs. 9,573 and treated the credit balance of Rs. 6,028 in favour of the branch as a remittance of profit into British India within the meaning of Section 4 (2) of the Income-tax Act as it stood before it was amended in 1939. The Income-tax Officer further held that as the assessee had not given any satisfactory explanation as to where he had kept the balance of Rs. 3,545, that sum must also be treated as profit received in British India :

Held, (*i*) *that, in the absence of any evidence, direct or circumstantial, the Income-tax Officer could not assume that the sum of*

Rs. 3,545 was brought into British India and could not assess it under Section 4 (2);

(ii) that the margin of profit added on at the branch when the goods were sent to the head office in British India could not be treated as profit earned outside British India;

(iii) that the Income-tax Officer was entitled to include in the income liable to tax the profit on the sale of the goods invoiced at Rs. 65,203 under Section 4 (1) only, and not under Section 4 (2) inasmuch as the head office and the branch were not two different legal entities and there was no legal liability on the part of the head office to pay the amount to its branch;

(iv) that the amount taxable should be based on the cost price which would include the price paid for the goods by the assessee together with the expenses for warehousing the goods and a certain amount for overhead charges at the branch.

There is no presumption either of fact or law that a person keeps all his income at his place of residence.

Case referred to :—

Commissioner of Income-tax, Bombay *v.* Ahmedabad Advance Mills Ltd. [1940] (8 I.T.R. 95; 67 I.A. 115; I.L.R. 1940 Bom. 332; A.I.R. 1940 P.C. 36; 185 I.C. 821).

Reference under Section 66 (1) of the Indian Income-tax Act (XI of 1922) by the Income-tax Appellate Tribunal: Miscellaneous Case No. 427 of 1942.

STATEMENT OF CASE.

"Messrs. Ram Lal Bechai Ram of Jaunpur have applied under Section 66 (1) of the Income-tax Act, 1922, requiring us to refer to the High Court of Judicature at Allahabad, a question which is claimed to be a question of law arising out of our order dated the 27th February 1942, in R. A. A. No. 13 (U. P.) of 1941-42.

2. The main business of the applicant is to deal in cloth. The head office is located at Semohi (British India) and there is a branch office at Bhadohi in Benares State. In his assessment order dated the 17th November 1939, for the assessment year 1938-39, the Income-tax Officer found that the entire profits earned in Benares State during the relevant accounting year were remitted to British India during that year " partly from remittances through the accounts and partly from suppressed cloth profits outside the accounts."

3. The Bhadohi shop (Benares State) profit was computed at Rs. 9,573. The Bhadohi shop account in the Semohi books showed that the receipts from Bhadohi exceeded the remittances to that place by Rs. 6,028. Actually, goods priced at Rs. 65,203-13-9 were sent to the head office in British India by the Bhadohi shop for which the Bhadohi shop was paid Rs. 59,175-13-0 only, leaving a credit balance of

Rs. 6,028 in favour of Bhadohi in the head office books. This credit balance was treated by the Income-tax Officer as a remittance of profits into British India in terms of Section 4 (2) of the Income-tax Act as it stood before it was amended in 1939. The Income-tax Officer held that over and above this amount further profits of the Bhadohi shop had been remitted to British India, in the shape of suppressed cloth profits, at least to the extent of the difference between the total profits earned, *viz.*, Rs. 9,573 and Rs. 6,028 credit balance in the name of the branch shop.

4. On appeal the Appellate Assistant Commissioner disagreed with the Income-tax Officer's finding and considered that the credit balance of Rs. 6,028 represented nothing but the price of goods which remained in arrears with the Semohi shop. In view of the fact that no cash remittances were made by Bhadohi shop and relying upon the Privy Council decision in *Commissioner of Income-tax, Bombay* v. *Ahmedabad Advance Mills Ltd.*[1], the Appellate Assistant Commissioner came to the conclusion that since the Bhadohi shop profits—declared or suppressed—were converted into goods and remitted to British India in that shape they could not be treated as income brought into British India under Section 4 (2) of the Act. The goods in question were described by the Appellate Assistant Commissioner as capital assets.

5. The Income-tax Officer preferred an appeal to the Tribunal against the Appellate Assistant Commissioner's order. An examination of the assessee's books of accounts disclosed that the prices at which the goods were supplied to the head office in British India included a profit margin and this fact was admitted by the assessee's munim. In essence the sale to the head office reflected the same trading results as a sale to a customer in Benares State would have done. When the goods were supplied to the head office at the sale price the sales account in the Bhadohi books was credited and the gross profit had been made. The goods sent to British India were admittedly sent for the purpose of resale and were in the nature of stock-in-trade. In our determination of the appeal by our order dated the 27th February 1942, we found as a fact that some Bhadohi profits were remitted to British India in the shape of marketable stock-in-trade. Relying upon the Privy Council decision in *Commissioner of Income-tax, Bombay* v. *Ahmedabad Advance Mills Ltd.*[1], referred to above, we concluded that such a remittance comes within the purview of Section 4 (2) of the Act as it stood before it was amended. The Commissioner of Income-tax in his reply filed under rule 54 of the Appellate Tribunal Rules contends that no question of law arises out of our

(1) (1940) 8 I.T.R. 95.

order dated the 27th February 1942, unless the sufficiency of the material upon which the findings of facts are based is questioned which in his opinion cannot be challenged. No such objection has, however, been taken by the appellant.

6. In our opinion the following question of law arises out of our order dated the 27th February 1942, which we refer for the opinion of the High Court:—

'Whether, in the circumstances of the case, the Income-tax Officer rightly included in the income liable to tax the profit on the sale of goods priced at Rs. 65,203-13-9 and the estimated profit of concealed sales to Semohi on the ground that though the said income accrued or arose without British India it was received or brought into British India within the meaning of Section 4 (2) of the Act, as it stood before its amendment in 1939.'"

K. N. Katju and *B. Upadhiya*, for the assessee.

G. S. Pathak, for the Commissioner.

JUDGMENT.

MALIK, J.—The facts of this case are very simple. Messrs. Ram Lal Bechai Ram, a trading undivided Hindu family, had their head office together with a cloth shop at Semohi in the Jaunpur district in British India. They maintained also a branch cloth shop at Bhadohi in the Benares State. They were residents of Jaunpur in British India. In their books at Bhadohi the firm maintained an account in the name of their own Semohi shop. Conversely in the Semohi books they had similarly an account in the name of the Bhadohi shop. From time to time goods were sent from one shop to the other. In the year in question, that is, in the assessment year 1938-39 it was found that cloth worth Rs. 65,203-13-9 was sent from the Bhadohi shop to the Semohi shop. The invoice price of these goods was not, however, their cost price to the Bhadohi shop but it included a profit margin equal to the profit that the Bhadohi shop would or might have derived from its customers in Bhadohi had the cloth been actually sold by that branch to customers in Benares State. In other words its own head branch in British India was notionally treated by the Bhadohi branch as its trading customer in the ordinary course of business. The Semohi shop remitted to its Bhadohi branch in the course of the same year sums amounting to Rs. 59,175-13-0 only, leaving a credit balance of Rs. 6,028 in favour of Bhadohi in the Semohi books.

The Income-tax Officer accepted the Semohi books as correct and assessed the assessee as regards the income derived from the sale of goods at Semohi on the basis of the entries made in the account books.

The Income-tax Officer, however, did not accept the Bhadohi books to be correct and made a best judgment assessment and came to the conclusion that the total profit earned by the Bhadohi shop was Rs.9,573. As the whole of the invoiced purchase price of Rs. 65,203-13-9 had not been transmitted by the Semohi shop to the Bhadohi shop in the course of the year, the Income-tax Officer held that the balance of Rs. 6,028 must be taken to be a profit which had accrued without British India and, in the sense that as goods or money it was still in British India, had been brought into British India within the meaning of Section 4 (2) of the Indian Income-tax Act (XI of 1922) before its amendment by the Indian Income-tax Amendment Act (VII of 1939). After having held that Rs. 6,028 out of the assessed profits of Rs. 9,573 was thus brought into British India, the Income-tax Officer went on to hold that the assessee had not given him any satisfactory information as to where he had kept Rs. 3,545, the balance of the assessed profit, after allowing for the above Rs. 6,028. In the absence of any information by the assessee the Income-tax Officer held that he was justified in presuming that the whole of the profit earned outside British India was received in British India. The Income-tax Officer thus assessed the assessee on the whole sum of Rs. 9,573 which, he held, was the profit earned outside British India.

The assessee appealed against this assessment under Section 30 of the Act. The Appellate Assistant Commissioner by his order dated March 25, 1942, held that no money had been transmitted from Bhadohi to Semohi, that only goods had been sent from one shop to the other and that the sum of Rs. 6,028 represented nothing but the price of goods which remained unpaid by the Semohi shop to the Bhadohi shop. Relying on the decision of their Lordships of the Privy Council in *Commissioner of Income-tax, Bombay* v. *Ahmedabad Advance Mills Ltd.*[1], he held that the amount was not taxable. He allowed the assessee's appeal and directed that the whole of the sum of Rs. 9,573 should be excluded from assessment.

The Income-tax department appealed against this decision before the Tribunal which held that the goods brought into British India were "stock-in-trade" which was meant to be resold at the first available opportunity, that they were not a capital asset and the decision of the Privy Council in the case of the Ahmedabad Mills was thus distinguishable. The Tribunal allowed and restored the order of the Income-tax Officer and held that the sum of Rs. 9,573 was taxable under Section 4 (2) of the Act as profits made outside British India and brought into British India.

(1) (1940) 8 I.T.R. 95.

The assessee then applied under Section 66 (1) of the Act for the statement of a case to this Court and formulated a question of law which reads as follows :—

"Whether, in the circumstances of the case, the Income-tax Officer has rightly included in the income liable to tax the amount of Rs. 9,573 on account of profits earned at Bhadohi in Benares State on the ground that though the said income accrued or arose in Benares State it was received or brought into British India within the meaning of Section 4 (2) of the Act."

This application was opposed by the department, but on October 24, 1942, the Income-tax Appellate Tribunal referred to us the following question for opinion :—

"Whether, in the circumstances of the case, the Income-tax Officer rightly included in the income liable to tax the profit on the sale of goods priced at Rs. 65,203-13-9 and the estimated profit of concealed sales to Semohi on the ground that though the said income accrued or arose without British India it was received or brought into British India within the meaning of Section 4 (2) of the Act, as it stood before its amendment in 1939."

We shall deal with the second part of the question first which relates to the estimated profit of concealed sales to Semohi. The question itself is not very clear, but from what we can gather from reading the various orders, it appears that this part of the question relates to the sum of Rs. 3,545 which was the balance after deducting Rs. 6,028 from Rs. 9,573 which was the total profit estimated by the Income-tax Officer as having been earned by the Bhadohi branch outside British India. The only question that arose in connection with this sum of Rs. 3,545 was whether, in the absence of any materials on the record, the Income-tax Officer was entitled to assume that it was a profit earned outside British India which was brought into British India. Learned counsel appearing for the department has argued that there is a presumption that a man keeps all his money at the place where he resides and in the absence of anything to the contrary, the Income-tax Officer's presumption was justified under Section 114 of the Indian Evidence Act which reads as follows :—

"The Court may presume the existence of any fact which it thinks likely to have happened, regard being had to the common course of natural events, human conduct and public and private business, in their relation to the facts of the particular case."

It is not said on behalf of the Income-tax department that there was any evidence on which the department could find that this sum of Rs. 3,545 was actually brought into British India, and we do not

consider that there is any presumption either of fact or of law that for income-tax purposes a man carries all his money with him wherever he goes. The assessee knew that, if he brought this money into British India, he would be liable to pay income-tax on it in British India. He was already subject to income-tax within the Benares State. In the absence of any evidence, direct or circumstantial, the Income-tax Officer could not assume that this amount was brought into British India and could not assess income-tax on it under Section 4 (2) of the Act, as it stood before its amendment in 1939. This is our answer to this part of the question.

The other part of the question which remains for decision reads as follows :—

"Whether, in the circumstances of the case, the Income-tax Officer rightly included in the income liable to tax the profit on the sale of goods priced at Rs. 65,203-13-9 on the ground that though the said income accrued or arose without British India it was received or brought into British India within the meaning of Section 4 (2) of the Act, as it stood before its amendment in 1939."

There is no difficulty in answering the first part of this question that the Income-tax Officer rightly included in the income liable to tax the profit on the sale of goods priced at Rs. 65,203-13-9. These goods, though brought from Bhadohi, were actually sold by the Semohi shop and the whole of the price was received in Semohi and there could be no manner of doubt that the Income-tax Officer was entitled under Section 4 (1) of the Income-tax Act, as it stood before its amendment in 1939, to tax the same as profits received in British India.

The second part of the question, if we may say so without meaning any disrespect to the Tribunal, really amounts to *false demonstration.* The income on the sale of the goods invoiced from Bhadohi to Semohi at Rs. 65,203-13-9 is certainly taxable but as we have already said, it is taxable not under Section 4 (2) but under Section 4 (1) of the Act. The reason to our minds is obvious. The Bhadohi shop and the Semohi shop were not separate legal entities. They belonged to the same assessee firm, Ram Lal Bechai Ram, an undivided Hindu family. These goods were purchased by the firm at a certain price none the less so, because they were taken in the first place to the Bhadohi shop and kept there. It must be admitted that the Bhadohi shop must have incurred some expenses in warehousing the goods and a certain apportioned amount of the overhead charges of the Bhadohi branch must be held attributable to them. That would be in proportion to the quantity of these goods to the quantity of the total turn-

over at Bhadohi. When these goods were sent from Bhadohi to Semohi and a margin of profit was added on to the price in the invoice could it be said that the Bhadohi shop earned this profit from the Semohi shop and that the cost price to the Semohi shop was the invoice price at which the goods were received by it from its own Bhadohi branch, and that thus the profit earned in Semohi was only the difference between the sale price at Semohi and the invoice price at which the goods had been received from Bhadohi. We think it is impossible to hold that a man can make a profit out of himself. If that were possible, then all that a businessman in British India need have done to escape payment of income-tax under Section 4 before the amendment of 1939 was to have a branch outside British India and when sending goods from the branch shop to the shop in British India to include in the invoice price such a margin of notional profit, which would make it certain that, in selling the goods in British India, he would make no profit, even though in fact his firm as a whole derived a large profit from the entire transaction. We put a question to learned counsel for the department to the effect that, if the assessee had spent Rs. 10,000 on the purchase of cloth at Bhadohi and had mentioned the invoice price as Rs. 15,000 when sending the cloth from Bhadohi to Semohi and had then sold it at Semohi for Rs. 13,000 could he be said to have made a profit of Rs. 3,000 or was he to be said to have incurred a loss of Rs. 2,000. The answer of course was that he had made a profit of Rs. 3,000. Even though the price of the cloth which was sent from Bhadohi to Semohi may have been paid from Bhadohi, the fact remains that the whole of the sale price of the cloth, the invoice price of which was Rs. 65,000 odd, was received in British India or would have been received in British India as soon as the goods were sold. The Income-tax Officer probably taxed the difference between the invoice price of Rs. 65,203-13-9 and the sale price in British India. But to our mind the amount taxable should have been based on the cost price, which would include, as we have already said, the price paid for these goods by the assessee, together with the apportioned expenses incurred by him for warehousing them, plus a certain amount for overhead charges at Bhadohi in proportion to the relation that these goods bore to the total turnover at Bhadohi. The profit or gain would be ascertained by deducting the whole of this sum from the price for which the goods were sold and in case any portion of the goods were not sold, by taking the difference in the stock as on the opening day and the last day and including that in the profit and loss account prepared to show the amount of the net profit of the assessee earned in British India

under Section 4 (1) of the Income-tax Act. In other words our view is that it could not be said that the margin of profit added on at Bhadohi when the goods were sent to British India could be treated as profit earned outside British India. The whole of the profit, ascertained as above, which accrued to the assessee by the sale of these goods must be deemed to be profit earned in British India, and these goods could not be taken separately as an isolated transaction but must be treated as part of the whole business of the firm spreading over the whole year. In the view that the department has taken of this case all that was necessary for the assessee was to remit the sum of Rs. 6,028 within the year to the Bhadohi shop to escape assessment for this amount. In an open and current account kept for the facility of accounting between the two shops belonging to the same proprietor, it is a matter of chance as to what is the balance that may remain due at any given moment from one to the other. It may vary from time to time and from day to day, and it is always a matter within the discretion of the head office when, if at all, the balance shall be adjusted. It does not even follow that it will ever be adjusted, since there could be no legal obligation on the Semohi branch ever to transmit money to its own Bhadohi branch. This type of business between one branch firm and another, even though they belong to the same proprietor, is not at all uncommon and, in our view, it is not the book balance that nominally remained due on March 31 that is the determining factor. We asked learned counsel for the department whether he was in a position to say that this amount was not transmitted from Semohi to Bhadohi on April 2. His answer was that he had no knowledge about it. It is true that according to the system of accounting between the two branches, the head office at Semohi did formally enter in its books an acknowledgment of its "liability" to pay this amount to its own branch at Bhadohi. But how the assessee, for the purposes of his accounts, keeps his books is not the test by which the liability to tax is concluded. We have to look to the substance of the transaction and, to our minds, we cannot accept the Bhadohi shop and the Semohi shop as two different legal entities, one able to earn a profit from the other. Nor can we accept it that there was any legal liability on the part of the Semohi shop to pay the amount to its Bhadohi branch. In the view that we have taken of this matter, our answer to the question must be that, in the circumstances of the case, the Income-tax Officer rightly included in the income liable to tax the profit on the sale of goods invoiced at Rs. 65,203-13-9. He was, however, entitled to do it only under Section 4 (1) of the Income-tax Act in the manner indicated by us above and not on the ground that, though the said income

accrued or arose without British India, it was received or brought into British India within the meaning of Section 4 (2) of the Act, as it stood before its amendment in 1939.

In the view that we have taken of the case we think that the department is not entitled to its costs and that the parties should bear their own costs. We assess the fee of the counsel for the department at Rs. 200 and give him six weeks within which to file a fee certificate. A copy of this judgment will be sent to the Tribunal and the Commissioner of Income-tax under the seal of the Court and the signature of the Registrar.

Reference answered accordingly.

[IN THE BOMBAY HIGH COURT.]

B. M. KAMDAR, *In re.*

SIR LEONARD STONE, C. J., KANIA and CHAGLA, JJ.

March 23, 1945.

INDIAN INCOME-TAX ACT (XI OF 1922), SECS. 10, 25—INCOME—DISCONTINUANCE OF PROFESSION IN ACCOUNTING YEAR—OUTSTANDING PROFESSIONAL FEES REALISED AFTER DISCONTINUANCE—WHETHER INCOME—WHETHER LIABLE TO INCOME-TAX.

The assessee who carried on a business of furniture maker and was practising as a consulting engineer sold his furniture business to a private limited company on February 15, 1938, and discontinued his practice as a consulting engineer from that day onwards. He was assessed for the assessment year 1939-40 (accounting year being calendar year 1938) on a certain sum which included Rs. 12,302 representing outstanding professional fees earned from his practice as a consulting engineer prior to discontinuance and realised by him during calendar year 1938. The assessee was keeping his accounts on the cash basis and he contended that as he had discontinued his profession in the accounting year 1938, the source had come to an end and the sum of Rs. 12,302 was not income liable to income-tax:

Held, *by* KANIA and CHAGLA, JJ., (STONE, C. J., dissenting), *that the sum of Rs. 12,302 less the permitted deductions under Section 10 of the Income-tax Act was income of the assessee liable to income-tax.*

Shaw Wallace and Company's Case [1932] (59 I.A. 206) *does not purport to state that if the payments were in respect of commission earned when the agencies subsisted, they were not income under Section 10.*

STONE, C. J.—*That portion of the outstanding fees which was received from January 1 to February 15 (both inclusive) ought to have been assessed under Section 25 of the Act, and, had they been, they would have been liable to income-tax, and the portion received on and from February 16 till the end of the calendar year was not assessable to income-tax.*

Cases referred to :—

B. C. G. A. (Punjab) Ltd. *v.* Commissioner of Income-tax, Punjab [1937] (5 I.T.R. 279 ; A.I.R. 1937 Lah. 338 ; I.L.R. 1937 Lah. 306 ; 168 I C. 549 ; 10 I.T.C. 298).

Behari Lal Mullick, *In re* [1927] (A.I.R. 1927 Cal. 553 ; 54 Cal. 630 ; 103 I.C. 609).

Bennett *v.* Ogston [1930] (15 Tax Cas. 374).

Brown *v.* National Provident Institution ([1921] 2 A.C. 222 ; 90 L. J. K. B. 1009 ; 125 L.T. 417).

Commissioner of Income-tax, Bombay *v.* Chunilal B. Mehta [1938] (6 I.T.R. 521 ; A.I.R. 1938 P.C. 232 ; I.L.R 1938 Bom. 752 ; 65 I.A. 332 ; 176 I.C. 15).

Commissioner of Income-tax, Madras *v.* Muthukaruppan Chettiar [1935] (3 I.T.R. 208 ; A.I.R. 1935 P.C. 117 ; 58 Mad. 881 ; 62 I.A. 203 ; 156 I.C. 671 ; 37 Bom. L.R. 815 ; 8 I.T.C. 338).

Commissioner of Income-tax *v.* Shaw Wallace & Co. [1932] (A.I.R. 1932 P.C. 138 ; 136 I.C. 742 ; 59 Cal. 1343 ; 59 I.A. 206).

Gopal Saran Narain Singh *v.* Commissioner of Income-tax, Bihar and Orissa [1935] (62 I.A. 207 ; 14 Pat. 552 ; 16 P.L.T. 531 ; A.I.R. 1935 P.C. 143 ; 42 L.W. 243 ; 156 I.C. 856 ; 3 I.T.R. 237 ; 37 Bom. L.R. 817 ; 8 I.T.C. 340).

Hillerns and Fowler *v.* Murray [1932] (17 Tax Cas. 77 ; 146 L.T. 474 ; 48 T.L R. 213).

Indian Iron and Steel Co., Ltd. *v.* Commissioner of Income-tax, Bengal [1943] (11 I.T.R. 328 ; A.I.R. 1943 P.C. 124 ; I.L.R. (1943) 2 Cal. 524 ; 70 I.A. 100 ; 208 I.C. 434 ; 48 C.W.N. 52).

Kamakshya Narain Singh *v.* Commissioner of Income-tax, Bihar and Orissa [1943] (11 I.T.R. 513 ; A.I.R. 1943 P.C. 153 ; 22 Pat. 713 ; 70 I.A. 180 ; 210 I.C. 1 ; 47 Bom. L.R. 545 ; 48 C W N. 59 ; (1943) 2 M.L.J. 410).

Probhat Chandra Barua *v.* Emperor [1930] (A.I.R. 1930 P.C. 209 ; 58 Cal. 430 ; 57 I.A. 228 ; 125 I.C. 871).

South Indian Industrials Ltd. *v.* Commissioner of Income-tax, Madras [1935] (A.I.R. 1935 Mad. 330 ; 58 Mad. 433 ; 157 I.C. 143 ; 3 I.T.R. 11).

Whelan *v.* Henning ([1926] A.C. 293 ; 95 L.J.K.B. 394 ; 134 L.T. 513).

Reference under Section 66 (2) of the Indian Income-tax Act (XI of 1922) by the Commissioner of Income-tax, Bombay, Sind and British Baluchistan : Income-tax Reference No. 12 of 1944.

STATEMENT OF CASE.

"1. Under Section 66 (2) of the Indian Income-tax Act, XI of 1922 (hereinafter referred to as "the Act"), and at the instance of Mr. B. M. Kamdar (hereinafter referred to as "the assessee") I have the honour to refer for your Lordships' decision the question stated in paragraph 6 below, which has arisen out of the income-tax and super-tax assessments of the assessee for the year 1939-40.

2. *Facts of the case.*—The assessee was the sole proprietor of a business run under the name "Kamdar Karyalaya" and was also

arrying on the profession of a consulting civil engineer in Bombay. 'he business of Kamdar Karyalaya was converted into a private limited ompany styled " Kamdar Limited " on the 15th of February 1938, and he assessee was appointed as " managing member " of the company. Jnder the terms of his agreement with the company he was to devote is time, attention and abilities to the business of the company and was to be paid a monthly salary of Rs. 1,500 plus a commission on the net profits. He was also to be provided with furnished residential quarters free of rent and with a motor car or at his option a monthly allowance of Rs. 500. A copy of the agreement is annexed and marked A.

3. On the 8th of September, 1939, the assessee submitted a return of income for the previous year ending on the 31st of December, 1938. In this return he included a sum of Rs. 12,302 under the head " business, profession or vocation." In the course of the assessment proceedings however he claimed that this sum was not in fact liable to taxation since he had ceased to do private professional work in view of the formation of the company and had not undertaken any such work during the relevant accounting period. The Income-tax Officer held that the income received from outstanding professional fees was liable to taxation and he completed the assessment on the following income:—

		Rs.
Salary	...	13,500
Profession	...	12,302
Dividends	...	378
Interest on loans	...	2,491
¼ share of income from the estate of Mr. M. M. Kamdar	...	6,060
		34,731

A copy of the assessment order is annexed and marked B.

4. On appeal the Appellate Assistant Commissioner made two minor modifications in the assessment. He reduced the salary income by Rs. 1,500 on the ground that the Income-tax Officer was not entitled to take into consideration the salary received after the 31st of December, 1938, but he added a sum of Rs. 1,000 on account of the value of rent-free quarters. Thus the net result was a reduction of Rs. 500 in the total income. As regards the taxability of the professional income the Appellate Assistant Commissioner upheld the decision of the Income-tax Officer. A copy of his order is annexed and marked C.

5. The assessee then filed an application under Sections 33 and 66 (2) of the Act in which he requested the Commissioner either to revise the assessment or to make a reference to the High Court. A copy of this application is annexed and marked D. Apart from the main question at issue the assessee has argued in his application that the Appellate Assistant Commissioner overestimated the value of the rent-free quarters. This is admittedly a question of fact and on the information at present available I consider that the Appellate Assistant Commissioner's estimate was reasonable, especially as under the terms of the agreement the quarters were to be fully furnished. The main question regarding the professional income is clearly a question of law, and as I am not prepared to revise the assessment I must accept the assessee's alternative request for a reference.

6. *Question for decision.*—I accordingly refer the following question for your Lordships' decision :—

" Whether, in the circumstances of the case, the outstanding professional fees which were realised by the assessee during the year under assessment are taxable as part of his income for that year ? "

7. *Opinion of the Commissioner.*—As has already been stated the private limited company styled Kamdar Ltd., came into existence on the 15th of February, 1938, and the assessee's obligation to devote his time, attention and abilities to the business of the company also has effect from that date. The Appellate Assistant Commissioner's finding is that "no new contract or work was undertaken after February, 1938." During the first six weeks of the calendar year 1938, which is the accounting period for this assessment, the assessee was in no way debarred from carrying on his profession, and it has not been established that he had in fact discontinued his profession before the beginning of that year.

8. But even if the assesseee did not undertake any new business in his personal capacity during the calendar year 1938 the department would still, in my opinion, be entitled to tax the professional fees which he received in that year. In claiming that these fees are not liable to taxation he relies mainly on the following observations made by Rowlatt, J., in the case of *Bennett* v. *Ogston* [1] :—

" When a trader or a follower of a profession or vocation dies or goes out of business......and there remain to be collected sums owing for goods supplied during the existence of the business or for services rendered by the professional man during the course of his life or his business, there is no question of assessing those receipts to income tax ; they are the receipts of the business while it lasted, they are arrears of

(1) (1930) 15 Tax Cas. 374.

that business, they represent money which was earned during the life of the business and are taken to be covered by the assessment made during the life of the business, whether that assessment was made on the basis of bookings or on the basis of receipts."

In my opinion these observations have no application to the present case since they depend on two features of the income-tax law in the United Kingdom which are absent from the Indian law. In the first place the English law requires the source of income to be in existence in the year of assessment whereas the Indian Income-tax Act does not contain any such requirement. In the second place the English law allows the assessing officer to refuse to accept the cash basis as a method of accountancy, and in actual practice in the case of newly set up professions where accounts are kept on the cash basis an attempt is made to arrive at the real profits by adding a proportion of the outstandings to the cash receipts of the year under assessment. Consequently according to the United Kingdom practice even in cases where accounts are kept on the cash basis the entire profits are assumed to have been assessed, and when a profession is discontinued there is *ex hypothesi* nothing more to assess. This explains the observation of Rowlatt, J., that the receipts in question are taken to be covered by the assessment made during the life of the business "whether that assessment was made on the basis of bookings or on the basis of receipts." In India the Income-tax Officer has to follow Section 13 of the Act and to compute the profits in accordance with the method of accounting regularly employed by the assessee. It has hitherto been assumed that under the Indian law the Income-tax Officer is not at liberty to refuse to accept the cash basis as a method of accounting and no attempt is made to add a proportion of the outstandings to the profits ascertained on that basis. Hence assessments made in India on the cash basis do not, like the assessments made in the United Kingdom, purport to include all the profits made during the life of the business.

9. It is clear that if the assessee had kept his accounts on the mercantile system the present question would not have arisen since the income in dispute would have been included in his assessments for the years in which it became due. The question arises only because he has in fact maintained his accounts on the cash basis and that basis has been accepted, under Section 13 of the Act, as a method of accounting regularly employed by the assessee. If the assessee's interpretation of the law were upheld a sum which clearly represents income from a profession would escape assessment merely because he has chosen to maintain his accounts on the cash basis. I submit that an

interpretation which produces this result cannot be correct. As Lord Trayner remarked in *Californian Copper Syndicate* v. *Harris*[1]: "I cannot think that income tax is due or not according to the manner in which the person making the profit pleases to deal with it."

10. As regards the assessee's contention that the amount in question is not "income" but the realisation of a debt I venture to point out that every sum received by him for professional services rendered while he was carrying on his profession was the realisation of a debt, but nevertheless it was admittedly income. I further submit that the treatment of bad debts relating to a discontinued business is not relevant to the present question since the admissibility of a bad debt as a set-off against the other income of an assessee is governed by the specific provisions of the Act. Under the scheme of the Act all income, profits and gains are liable to taxation unless specifically exempted, and even if the income in question were held not to be taxable under the head "business, profession or vocation" it would still in my opinion be taxable under "other sources."

11. So far as I am aware there is no recorded ruling on an exactly similar case, but I venture to invite a reference to the Privy Council's decision in *Commissioner of Income-tax, Madras* v. *P.R.A.L. Muthukaruppan Chettiar*[2], which related to the somewhat analogous question of a partner's share in the profits of a discontinued business. It was held that the amount received by the partner was a payment of profits and had been properly assessed in the year of receipt.

12. For the above reasons I am respectfully of opinion that the question which has been stated should be answered in the affirmative."

Sir Jamshedji Kanga, for the assessee.

M. C. Setalvad, for the Commissioner.

JUDGMENT.

STONE, C. J.—This is a reference under Section 66 (2) of the Indian Income-tax Act, 1922, and comes to us direct from the Commissioner under the option given to the assessee by the 1940 Act. The reference arises out of an assessment to income-tax upon the assessee for the assessment year 1939-40 in respect of the accounting year previous, which in this case is the calendar year 1938.

The assessee was assessed to income-tax by an assessment order dated March 23, 1939, in a total sum of Rs. 34,731, made up, as the assessment order shows, of income from four sources, namely salary (director's remuneration), profession, interest and a one-third share from the estate of a Mr. Kamdar. The item in dispute is Rs. 12,302,

(1) (1904) 5 Tax Cas. 159. (2) (1935) 3 I.T.R. 208.

which, in the assessment order, is described as: "Profession-Recoveries from outstandings during calendar year 1938 as per bill-book."

Before February 15, 1938, the assessee had carried on the business of a furniture dealer under the name of "Kamdar Karyalaya," and he also carried on a professional practice as a consulting engineer. On February 15, the assessee sold his furniture business to a limited company which had been formed for the purpose of taking it over. Under the terms of the agreement for sale, the assessee agreed to devote the whole of his time and attention and abilities to the business of the company; and, at any rate, on February 15, 1938, if not before, his practice of a consulting engineer had been wholly discontinued. The exact date of such discontinuance is in some doubt, but in this Court it was agreed by counsel that February 15, 1938, should be taken as the date of discontinuance. The sum of Rs. 12,302 represents the assessee's outstanding professional fees earned from his practice as a consulting engineer previously to January 1, 1938, and paid to or received by the assessee during the calendar year 1938. It follows that, if a certain view of this matter was taken, the sum of Rs. 12,302 would have to be apportioned in order to discover how much of it was in fact received on or before February 15, 1938.

The question referred to us is as follows:—

"Whether, in the circumstances of the case, the outstanding professional fees which were realised by the assessee during the year under assessment are taxable as part of his income for that year?"

This question is misleading, as the expression "the year under assessment" is used not in the sense of the assessment year, which was 1939-40, long before which the business had been discontinued and in which no part of Rs. 12,302 was received, but the previous year, that is to say, the accounting year 1938.

The industry of counsel, to whose clear and able arguments we are much indebted, has not discovered any decision under the Indian Income-tax Act as to the outstanding fees which come in after the discontinuance of the practice by retirement of a professional man who keeps his books on a cash basis. In spite of Section 25 of the Act, to which I will refer later, it appears to have been assumed by the Income-tax authorities that such fees are liable to be brought to tax in the subsequent year. To quote from the opinion of the Commissioner of Income-tax in this case: "a sum which clearly represents income from a profession would escape assessment merely because he has chosen to maintain his accounts on the cash basis."

When this matter came before my brother Kania and myself, we felt considerable difficulty in discerning from the cross currents set up

by the divers facts of the decided cases in which the nature of income taxable under the Indian Act has been considered, any principle which would cover the important question, which arises for decision on this reference, and accordingly the reference has been re-argued before this Full Bench. It is with regret that I find myself compelled to take a different view of this matter from that taken by my learned brethren, and it is, therefore, not without diffidence that I shall proceed to give my reasons for the conclusion to which I have come, as the result of the arguments which have been addressed to us and an exhaustive examination of the Act itself and of the cases in which the nature of taxable income has been considered. To my mind this complex question admits of a simple answer, namely, that in the circumstances of the case the receipt after the discontinuance of the profession of outstanding fees is not income, profits or gains to which the Act applies.

It will be convenient, in the first place, to examine and consider the relevant sections of the Act and then to refer to certain reported cases in which the Judicial Committee of the Privy Council has expressed opinions on the structure and scheme of the Indian Act and upon the nature of the income taxable under it. At the outset, however, it should be observed that it is the Indian Act after the 1939 amendments had been introduced with which we have to deal, whereas all the cases, which have come before the Judicial Committee and to which we have been referred, are concerned with the 1922 Act as amended from time to time, but before the 1939 amendments came into operation.

Section 3 provides that "where any Act of the Central Legislature enacts that income-tax shall be charged for any year at any rate or rates, tax at that rate or those rates shall be charged for that year in accordance with, and subject to the provisions of, this Act in respect of the total income of the previous year of every individual, Hindu undivided family, company and local authority, and of every firm and other association of persons or the partners of the firm or members of the association individually."

"Total income" is defined by sub-section 2 (15) of the Act as follows :—

"'Total income' means total amount of income, profits and gains referred to in sub-section (1) of Section 4 computed in the manner laid down in this Act."

Turning to sub-section 4 (1), it is in these terms :—

"Subject to the provisions of this Act, the total income of any previous year of any person includes all income, profits and gains from whatever source derived which—

(*a*) are received or are deemed to be received in British India in such year by or on behalf of such person, or

(*b*) if such person is resident in British India during such year,—

(*i*) accrue or arise or are deemed to accrue or arise to him in British India during such year, or

(*ii*) accrue or arise to him without British India during such year, or

(*iii*) having accrued or arisen to him without British India before the beginning of such year and after the 1st day of April, 1933, are brought into or received in British India by him during such year, or

(*c*) if such person is not resident in British India during such year, accrue or arise or are deemed to accrue or arise to him in British India during such year."

These sub-sections are followed by a number of provisos and explanations, which principally concern the position when income arises outside British India. Sub-section (3) exempts from taxation certain classes of income, such as income from charities and agricultural income.

Section 4 completes Chapter I, which is intituled "Charge of Income-tax."

Chapter II is concerned with "Income-tax authorities."

Section 6 heads Chapter III "Taxable Income," and is as follows :—

"6. Save as otherwise provided by this Act, the following heads of income, profits and gains, shall be chargeable to income-tax in the manner hereinafter appearing, namely :—

(*i*) Salaries.

(*ii*) Interest on securities.

(*iii*) Income from property.

(*iv*) Profits and gains of business, profession or vocation.

(*v*) Income from other sources."

Section 7 deals with "Salaries"; Section 8 with "Interest on securities"; Section 9 with "Income from property"; whilst Sections 10 and 12, with which we are particularly concerned, deal respectively with "Profits and gains of business, profession or vocation" and "Income from other sources." Section 11, which formerly dealt with "Professional earnings," has been dropped by the 1939 amendments, which have enlarged the ambit of Section 10 so as to cover "business, profession or vocation."

The other relevant sections are: Section 13, which makes the method by which accounts are kept of a business, profession or vocation of material importance; Section 24, which provides for the set-off of losses under one head of Section 6 against gains under one of

the other heads; Section 25, which is permissive and provides what may be done when a business or profession is discontinued.

Section 10 is as follows :—

"(1) The tax shall be payable by an assessee under the head 'Profits and gains of business, profession or vocation' in respect of the profits or gains of any business, profession or vocation carried on by him.

(2) Such profits or gains shall be computed after making the following allowances, namely :— "

There follow, set out in numbered sub-paragraphs, a number of items of disbursement, such as rent, repairs, interest on capital borrowed for the purposes of business, premiums on insurance and depreciation, implemented by provisos and explanations.

Section 12 is as follows :—

"(1) The tax shall be payable by an assessee under the head 'Income from other sources' in respect of income, profits and gains of every kind which may be included in his total income (if not included under any of the preceding heads).

(2) Such income, profits and gains shall be computed after making allowance for any expenditure (not being in the nature of capital expenditure) incurred solely for the purpose of making or earning such income, profits or gains, provided that no allowance shall be made on account of—"

This time there follow sub-paragraphs explanatory of the excluded allowances.

Section 13 provides :—

"Income, profits and gains shall be computed, for the purposes of Sections 10 and 12, in accordance with the method of accounting regularly employed by the assessee :

Provided that, if no method of accounting has been regularly employed, or if the method employed is such that, in the opinion of the Income-tax Officer, the income, profits and gains cannot properly be deduced therefrom, then the computation shall be made upon such basis and in such manner as the Income-tax Officer may determine."

In this case the assessee regularly kept his accounts on a cash basis, and there has been no challenge to the propriety of his methods. Section 24 makes provision for the setting off of losses sustained under one of the heads of Section 6 against profits made under another head of that section. The section is :—

"(1) Where any assessee sustains a loss of profits or gains in any year under any of the heads mentioned in Section 6, he shall be entitled to have the amount of the loss set off against his income, profits or gains under any other head in that year."

Again, there follow a number of provisos with regard to the setting off of losses. Section 25 is as follows:—

"(1) Where any business, profession or vocation on which income-tax was not at any time charged under the provisions of the Indian Income-tax Act, 1918, is discontinued in any year, an assessment may be made in that year on the basis of the income, profits or gains of the period between the end of the previous year and the date of such discontinuance in addition to the assessment, if any, made on the basis of the income, profits or gains of the previous year.

(2) Any person discontinuing any such business, profession or vocation shall give to the Income-tax Officer notice of such discontinuance within fifteen days thereof, and, where any person fails to give the notice required by this sub-section, the Income-tax Officer may direct that a sum shall be recovered from him by way of penalty not exceeding the amount of tax subsequently assessed on him in respect of any income, profits or gains of the business, profession or vocation up to the date of its discontinuance."

Sub-section (3) deals with the discontinuance of business, profession or vocation which was charged under the provisions of the Indian Income-tax Act, 1918, and it provides that, except in the case of a succession, no tax shall be payable in respect of the income, profits and gains of the period between the end of the previous year and the date of such discontinuance, and also provides that the assessee may further claim that the income, profits and gains of the previous year shall be deemed to have been the income, profits and gains of the said period. No regard has been paid to this section in the assessment of the assessee to tax. No assessment has been made under it for the fraction of the year January 1 to February 15, 1938 (both inclusive). No reliance has been placed upon its operation by the Commissioner of Income-tax. Indeed there is nothing to show whether tax was charged on the profession under the provisions of the Indian Income-tax Act, 1918, or not.

Looking at the scheme of the early sections, the salient features of the 1939 Act are, as it seems to me, that under Section 3 tax is to be charged for any particular assessment year in respect of the total income of the previous year, which, by the conjoint effect of sub-section 2 (15) and Section 4, is the total amount of income, profits and gains (including all income, profits and gains from whatever source derived) which are received or are deemed to be received in British India or which accrue or arise or are deemed to accrue or arise in British India in the accounting year computed in the manner laid down in the Act. Three matters relevant to this apparently simple arrangement must be noticed. First, that income is nowhere defined, so that the search for a definition of it, which has agitated economists

and lawyers wherever a civilized order of society exists, is presented in all its unsatisfying perplexities by the Indian Act. Secondly, that the manner of computation laid down by the Act forms an integral part of the definition of "total income." Computation, it is to be observed, does not form a part of the charging section, but is introduced into the definition of the total income to be brought to tax. Thirdly, that both Sections 3 and 4 are expressly made "subject to the provisions of this Act."

What is chargeable to tax is the total amount of income, profits and gains circumscribed by three ideas, that is to say, the irrelevance of derivative sources, the connection with India and computation as laid down by the Act.

The charge of tax never operates upon a gross amount. The correlation of the three words, income, profits and gains makes this clear, for although income may be either gross or net, both profits and gains presuppose that the expenditure laid out in order to produce them has already been defrayed.

It is not, in my opinion, the correct method of approach to say that what is charged to tax by Sections 3 and 4 are gross receipts and that you then distribute those gross receipts to the appropriate heads of income in Section 6 throwing into "other sources" anything that will not fit the four preceding heads: all this being for the purpose of ascertaining the proper allowances and deductions to be made under each head, so that the truncated total of gross receipts remaining is the taxable balance. The correct method of approach in my judgment is to treat nothing as being charged to tax until by the process of computation laid down by the Act, the status of income, profits and gains emerges. If this be the correct approach, then what is taxable under the Act is something capable of being processed by the machinery of computation laid down by the Act for inclusion in what the Act describes as the total amount of income, profits and gains.

The fees outstanding from time to time of a professional man, who admittedly keeps his books on a cash basis, must, for the purpose of being processed to income, profits and gains, come either under head (*iv*) "Profits and gains of business, profession or vocation," dealt with by Section 10, or under head (*v*) "Income from other sources," dealt with by Section 12. Section 13 is mandatory: income, profits and gains *shall be computed*, for the purposes of Sections 10 and 12, in accordance with the method of accounting regularly employed by the assessee—in this case the cash basis. The nexus between it and sub-section 2 (15) is not unimportant.

Under Section 10 the profits and gains must be from a business, profession or vocation carried on by the assessee, and from these profits

or gains certain stated allowances are to be deducted. Do the words "carried on by him" mean carried on by the assessee in the assessment year or the accounting year, or do they mean carried on by the assessee at any time? If the latter, it would be difficult to find a terminal point; since even if the profession was in fact terminated, so long as there was a single outstanding fee, the profession would still notionally be "carried on," so that in any future assessment or accounting year in which an outstanding fee was received, there would have to be a head of assessment under Section 10 of the Act. If so, the assessee must be entitled to any permissible allowances, deductions and set-offs mentioned in sub-section 10 (2) and Section 24 in order that his total income might be computed under the Act, so that if on the termination of the profession there are outstanding debts of the profession which come within the permitted deductions, they would have to be brought into computation in the year in which they were actually paid, *e.g.*, by sub-section 10 (2) (iii) the amount of interest in respect of capital borrowed for the purposes of the profession, if such capital were not paid off before or upon the determination of the profession, would be a permissible deduction in future years, and if this exceeded the amount of outstanding fees received in any such future year, it must follow that under Section 24 this loss would be set off against other heads of income as if the profession was still being carried on. To quote again from the Income-tax Officer's opinion:

"The assessee was accounting for his income on cash basis. Hence, he must necessarily recover the outstandings till they are exhausted and until these are exhausted the business is deemed to have continued."

There does not appear to me any justification in the Act for artificially continuing a non-existing profession in this way. In my judgment, for a receipt to be assessable to tax under Section 10 it must be a receipt in respect of an existing business, profession or vocation capable of being processed to profits or gains by the method of computation laid down by Section 10. The Act itself has solved the problem of professions which are discontinued by Section 25. Why advantage of that section was not taken in this case by the Income-tax authorities it is difficult to understand except on the ground that the Crown was not satisfied with tax on that portion of the fees received between January 1 and February 15 (both inclusive), which under Section 25 could clearly have been assessed to tax and which were receipts of the profession while the profession was still being carried on.

Turning then to Section 12, are the outstanding fees when received "income from other sources?" In order to be so, it would mean that some new source of income, profits or gains sprang up either on

January 1 or on February 16, 1938, composed of the fees then outstanding. So far as the fees received on and between January 1 and February 15 are concerned, this clearly is not the case. The profession was then being carried on and these receipts, less the proper allowances, could, and, in my opinion, should have been assessed by the conjoint operation of Sections 10 and 25. On February 15 the profession ceased and according to the assessee's method of accounting there was left over a list of book-debts owed by debtors who were in arrear in the payment of their fees. In my opinion, having regard to the method of accounting employed by the assessee, these debts when collected are not income from other sources. There is nothing continuous about them and they are incapable of repetition, and the very fact that Section 25 is wholly silent with regard to them, though it deals with the situation in which they arise, negatives, in my opinion, their assessability to tax.

Before referring to the decided cases, some of the changes wrought by the amending Act of 1939 must be noticed. In new sub-section 2 (15) reference to sub-section 4 (1) is introduced in lieu of the words "from all sources to which this Act applies" and the important words, "computed in the manner laid down in this Act," are substituted for the words "computed in the manner laid down in Section 16." The scope of old Section 16 is of very limited operation. In new Section 3, tax is to be charged "in respect of the total income," whereas formerly tax was charged "in respect of all income, profits and gains." The consequential changes in Section 4 are no less important. The new words, "Subject to the provisions of this Act," are substituted for the old words "Save as *hereinafter* provided, this Act shall apply." I have already noticed the amendment to Section 6. The amendment to Section 12 harmonizes with the amendments referred to above. By the new section, tax is payable in respect of "income, profits and gains of every kind *which may be included in his total income*," whereas formerly it was payable in respect of "income, profits and gains of every kind and from every source to which this Act applies."

In my opinion, these amendments are material and must be borne in mind in any consideration of the cases which have been decided under the Act of 1922.

The first case is *Probhat Chandra Barua* v. *The King-Emperor*[1]. In that case certain receipts were held not to be agricultural income so as to exempt them from taxation under the Act. Lord Russell of Killowen, delivering the judgment of the Board, considered the scheme of the Act and said :—

(1) (1930) 57 I. A. 228, p. 238.

"It would appear that the purpose of Section 3 is to charge income-tax at the current rate for the time being, and that the purpose of Section 4 is [by sub-section (1)] to confine the tax to income actually or artificially accruing or arising or received in British India, and [by sub-section (3)] to exempt specified classes of income from tax.

Athough Chapter I is entitled 'Charge of income-tax,' the real charging section would appear to be Section 6, which occurs in Chapter III."

Having stated that the income of a zamindar would not be chargeable under the head "property," and that if chargeable it would be under the head "other sources," his Lordship continued :—

"Section 12 deals with that head, and requires close attention. Section 12, sub-section (1), provides that the tax shall be payable by an assessee under that head 'in respect of income, profits and gains of every kind and from every source to which this Act applies (if not included under any of the preceding heads).' These words appear to their Lordships clear and emphatic, and expressly framed so as to make the sixth head mentioned in Section 6 describe a true residuary group embracing within it all sources of income, profits and gains provided the Act applies to them, *i.e.*, provided that they accrue or arise or are received in British India or are deemed to accrue or arise or to be received in British India, as provided by Section 4, sub-section (1), and are not exempted by virtue of Section 4, sub-section (3)."

Dealing with the incidence of taxation, his Lordship observed :—

"The tax is upon 'income, profits and gains.' It is not a tax on gross receipts. With this fact in view, each section which deals with one of the first five 'heads' specified in Section 6 contains, where proper, specific provisions for the necessary deductions and allowances to be made for the purpose of arriving at the taxable balance. Section 12, which deals with the general residuary group, is necessarily framed in general terms and authorises the allowance of any 'expenditure (not being in the nature of capital expenditure) incurred solely for the purpose of making or earning such income, profits or gains.'"

The next case is *Commissioner of Income-tax* v. *Shaw Wallace & Co.*[1] In that case the assessee-company, which carried on the business of distributing agents in India for two oil companies, received from each of those companies a solatium on the termination of the inter-company arrangements; and the question was whether the sums thus paid by the two oil companies were liable to income-tax in the hands of the

(1) (1932) 59 I. A. 206; 59 Cal. 1343.

assessee-company. One of the questions formulated in the reference was (page 211):—

"If it could be said to be income, profits or gains within the meaning of the Act, was it liable to be assessed under either of the Sections 10 and 12 of the Act, inasmuch as (1) it was not the profits or gains of any business carried on by the assessees within the meaning of Section 10 of the Act, nor (2) income, profits or gains from other sources within the meaning of Section 12 of the Act?"

In delivering the judgment of the Board, Sir George Lowndes said (page 212):—

"The object of the Indian Act is to tax 'income,' a term which it does not define. It is expanded, no doubt, into 'income, profits and gains,' but the expansion is more a matter of words than of substance. Income, their Lordships think, in this Act connotes a periodical monetary return 'coming in' with some sort of regularity, or expected regularity, from definite sources. The source is not necessarily one which is expected to be continuously productive, but it must be one whose object is the production of a definite return, excluding anything in the nature of a mere windfall. Thus income has been likened pictorially to the fruit of a tree, or the crop of a field. It is essentially the produce of something which is often loosely spoken of as 'capital.' But capital, though possibly the source in the case of income from securities, is in most cases hardly more than an element in the process of production."

Having referred to and quoted Section 6 of the Act, his Lordship continued:—

"The claim of the taxing authorities is that the sum in question is chargeable under head (iv) business. By Section 2, sub-section (4), business 'includes any trade, commerce or manufacture, or any adventure or concern in the nature of trade, commerce or manufacture.' The words used are no doubt wide, but underlying each of them is the fundamental idea of the continuous exercise of an activity. Under Section 10 the tax is to be payable by an assessee under the head business 'in respect of the profits or gains of any business *carried on by him.*' Again, their Lordships think, the same central idea: the words italicised are an essential constituent of that which is to produce the taxable income: it is to be the profit earned by a process of production. And this is borne out by the provision for allowances which follows. They include rent paid for the premises where the business is carried on; the cost of current repairs in respect of such premises; interest on money borrowed for carrying on the business, etc."

And later his Lordship observed:—

"Their Lordships will only add that the reasoning of this judgment would apply equally if the appellant based his claim on head (vi) 'other sources' and the corresponding provisions of Section 12."

There followed in 1935 the case of *Commissioner of Income-tax, Madras* v. *Muthukaruppan Chettiar*[1]. In that case the assessee was the partner in a money-lending business, and on dissolution his share of the profits was paid to him in Colombo outside British India. Interest on capital amounting to Rs. 38,305 together with a greater part of the capital sum due was however paid to him in Madras; and the question arose: Whether this sum thus received in British India as interest on capital was a capital receipt or income assessable to tax. Lord Atkin, delivering the judgment of the Judicial Committee, said (page 210) :—

"The account taken on dissolution ascertains what is due to the partners for profits, and what is due for capital. It can hardly be suggested that the partners share according to their capital proportions in the whole assets of the partnership. This sum due for undrawn profits was and remains a sum due by the partners to each partner: and necessarily ranks first before the sums due for capital can be distributed. In other words, on dissolution of a partnership, an outgoing partner has the right to receive not as in the case of a shareholder in winding up a company only a share of the assets: but to receive payment of his profits, profits which were his before dissolution and do not cease to be his on dissolution. In their Lordships' opinion, the respondent received this payment in India as a payment of profits and was properly assessed."

Later in the judgment their Lordships point out that their decision did not cover cases where undrawn profits had, with the consent of all parties, been invested in the business so as to increase the capital account; nor had they had to consider any special provisions of the partnership articles which might affect the matter.

The next case is *Commissioner of Income-tax, Bombay Presidency and Aden* v. *Chunilal B. Mehta*[2]. In that case the assessee, who carried on business as a broker in Bombay, entered into certain future delivery contracts for the purchase and sale of commodities in various foreign markets from parties outside British India. No delivery was either given or taken, and the profits of such contracts were not received in British India. Sir George Rankin delivering the judgment of the Board said (pages 347-348) :—

"Their Lordships do not consider that the Indian Income-tax Act is patent of this construction. They will first deal with the argument based on Sections 4 and 6, that the respondent's business is the source

(1) (1935) 3 I.T.R. 208. (2) (1938) I.L.R. 65 I.A. 332 ; 6 I.T.R. 521.

of the profits, and that the sections require that the situation of the source should determine the place where the profits arise. This, in their Lordships' view, is a straining of the sections. The effect of Section 6 is to classify profits and gains under different heads for the purpose of providing for each appropriate rules for computing the amount; its language is 'shall be chargeable . . . . in the manner hereinafter appearing.' One of the heads is 'Business,' which as a head of income stands alongside Salaries, Interest on securities, Professional earnings, and Other sources. True, the classification of income is according to the character of the source, and it has been held that 'income, profits and gains' as distinct from casual receipts and from other forms of receipt or enrichment, involve the idea of a periodical money return from a definite source: (*Commissioner of Income-tax* v. *Shaw Wallace & Co.*[1]). It may further be said that sub-section (1) of Section 4 having used the word or notion 'source', the words which follow 'accruing or arising' are language in consonance therewith. But the list of 'heads' in Section 6 is a list of sources not in the sense of attributing the income to one property rather than another, one business rather than another, but only in the sense of attributing it to property as distinct from employment, or business as distinct from investment. Sections 4 and 6, taken together, say of business profits that they are taxable on certain conditions stated in Section 4 and in a manner to be laid down in a later section. When one comes to that section (Section 10) and not before, a further idea is introduced. 'The tax shall be payable by an assessee under the head 'Business' in respect of the profits or gains of any business carried on by him.' What is to be learnt from an examination of the language of sub-section (1) of Section 4—'income, profits or gains, as described or comprised in Section 6, from whatever source derived'—is that Section 6 is intended as describing different kinds of profit, and that if the condition 'accruing or arising or received in British India, etc.,' is satisfied by the profits, they will not escape by reason of any quality or circumstance of the source. There may be room for the view that, having regard to the sixth head in Section 6, the words 'from whatever source derived' are surplusage: even so, they are not there as a guide to the place where profits accrue or arise, but to make clear that for another purpose source is irrelevant. There is every presumption that in such a section in an Indian Act the legislature intends the exact language of the section to be the test of liability. To answer the question, 'Do these profits accrue or arise in British India?' by asking another, 'What in the sense of Section 6 is the source of these profits, and is it

(1) (1932) L.R. 59 I.A. 206.

situate in British India ?' is to divert attention from that to which the statute points and to devote attention to what it discards."

Though the last two cases to which I desire to refer are both reported in the 1943 volume of the Income Tax Reports, they both deal with the position before the 1939 Amending Act.

The first of those cases is *Indian Iron & Steel Co., Ltd.* v. *Commissioner of Income-tax, Bengal*[1]. The assessee-company agreed to acquire and take over the whole of the property of another company as existing on the date of transfer, which was December 2, 1936, and the assessee-company continued the business which it purchased in conjunction with its own existing business. Both companies had to their respective credit large sums of unabsorbed depreciation allowance which, under the Act, they could set off against future profits. December 2, 1936, came within the accounting period, which was from April 1, 1936, to March 31 following, and it was held that the purchaser-company was not entitled to have the depreciation allowance of the vendor-company computed on the original cost of the assets of the vendor-company for the whole of the previous year but only up to the date of succession. Lord Porter delivering the judgment of the Board said (page 336) :—

"Indian income-tax is assessed and paid in the next succeeding year upon the results of the year before. If then company A sold its business to company B in the first of the two years, apart from the provisions of Section 26 (2), the former company could not be assessed and would not be liable for any profits it then made, because it would not be carrying on the business in the next year for which in the normal course the assessment would be made and in respect of which tax would be due, nor would company B be liable except for any period during which it had itself owned the business and made profits, because the tax under Section 10 (1) is only 'payable by an assessee under the head 'business' in respect of the profits or gains of any business carried on by him.' "

The remaining case is *Kamakshya Narain Singh* v. *Commissioner of Income-tax*[2]. That case concerned the assessability to tax of certain royalties, and delivering the judgment of the Board Lord Wright, having dealt with the nature of the mining lease and the rights of the lessee thereunder and having referred, without approval, to the pictorial simile of 'income' given in the *Shaw Wallace case*[3], stated (page 523) :—

" There is, therefore, in their Lordships' judgment, no real justification for treating the royalties as capital payments. They think

(1) (1943) 11 I.T.R. 328.
(2) (1943) 11 I.T.R. 513.
(3) (1932) 59 I.A. 206.

that they are 'income' within the meaning of the Act, whatever may be the exact definition of that word in the Act. Its applicability may, in particular cases, differ because the circumstances, though similar in some respects, may be different in others. Thus the profit realised on a sale of shares may be capital if the seller is an ordinary investor changing his securities, but in some instances at any rate it may be income if the seller of the shares is an investment or an insurance company. Income is not necessarily the recurrent return from a definite source, though it is generally of that character. Income again may consist of a series of separate receipts, as it generally does in the case of professional earnings. The multiplicity of forms which 'income' may assume is beyond enumeration. Generally, however, the mere fact that the income flows from some capital assets, of which the simplest illustration is the purchase of an annuity for a lump sum, does not prevent it from being income, though in some analogous cases the true view may be that the payments, though spread over a period, are not income, but instalments payable at specified future dates of a purchase price."

The arguments and submissions of counsel have in large measure ranged round these cases in endeavours to show that one or some of them are decisive of the case before us. But when all has been said, the basic question is, whether the receipt of these outstanding fees after the profession has been discontinued are taxable income. It seems to me that the view I take is consistent with these authorities. In the language used by Lord Russell of Killowen in delivering the judgment in *Probhat Chandra Barua* v. *The King-Emperor*[1], "it is not a tax on gross receipts," and the sum of Rs. 12,302 in the case before us is unquestionably made up of gross receipts; it is not a "taxable balance."

Even if the pictorial simile to be found in the judgment in the case of *Commissioner of Income-tax* v. *Shaw Wallace & Co.*[2] is to be discarded, the Rs. 12,302 can be tested in the light of the observations in that case. It does not comply with "the fundamental idea of the continuous exercise of an activity;" nor can any part of the Rs. 12,302 come within "the same central idea" being "in respect of the profits or gains of any business *carried on by him*," except such part of the Rs. 12,302 as was received on or before February 15, 1938.

The case of *Commissioner of Income-tax, Madras* v. *Muthukaruppan Chettiar*[3] is, in my opinion, not in point, because in that case what was brought into British India were profits, profits existing and which

(1) (1930) 57 I.A. 228.
(2) (1932) 59 I.A. 206.
(3) (1935) 3 I.T.R. 208.

were the assessee's before the dissolution of the partnership firm, so that they in fact represented a taxable balance and not a gross receipt.

The case of *Commissioner of Income-tax, Bombay* v. *Chunilal B. Mehta*[1] dealt with the geographical quality of the source and not with the nature or composition of the receipt, which, apart from the question of source, was admittedly a profit and a profit from the continuous exercise of an activity.

The case of *Kamakshya Narain Singh* v. *Commissioner of Income-tax*[2] is strongly relied upon by Mr. Setalvad in his argument on behalf of the Crown, but the nature of the receipts in that case, royalties derived by virtue of a mining lease, and the receipt of outstanding fees in the case before us, are fundamentally different. The passage in the judgment delivered by Lord Wright that "Income is not necessarily the recurrent return from a definite source, though it is generally of that character," shows that there may be exceptions to any comprehensive definition of "taxable income" which may be attempted. Indeed, that case makes it clear that what may be taxable income when received by one man would be a capital receipt in the hands of another. It is the circumstances of each case which must be examined in the light of the general scheme and the specific provisions of the Indian Income-tax Act.

Various cases decided in the High Courts in India were referred to in the arguments before us. *South Indian Industrials, Ltd., Madras* v. *Commissioner of Income-tax, Madras*[3] and *B. C. G. A. (Punjab) Ltd.* v. *Commissioner of Income-tax, Punjab*[4], are in favour of the view which I take of this problem. On the other hand, a Full Bench decision in Calcutta, *Behari Lal Mullick, In re*[5], is to the contrary. Having regard to the decisions in the Privy Council already referred to, I do not think it would be profitable to enter into any exhaustive discussion on the Indian decisions. In my judgment the answer to the question referred to us in this case is that that portion of these outstanding fees which was received from January 1 to February 15 (both inclusive) ought to have been assessed under Section 25 of the Act, and, had they been, they would have been liable to income-tax and that the balance being that portion received on and from February 16 till the end of the calendar year is not assessable to income-tax. In deference to the able arguments that have been addressed to us, there are two further aspects of the matter which I desire to mention. Although in my judgment, the primary answer to the question in this case is,

(1) (1938) 65 I.A. 332 ; 6 I.T.R. 521.
(2) (1943) 11 I.T.R. 513.
(3) (1935) 3 I.T.R. 11 ; 58 Mad. 433.
(4) (1937) 5 I.T.R. 279.
(5) (1927) 54 Cal. 630.

that outstanding fees which come in after the determination of the profession which earned them are not receipts capable of computation as income, profits or gains within the meaning of the Act, the question can also be answered by saying that having regard to the terms of Section 13 tax has notionally already been paid in respect of the outstanding fees during the continuance of the business.

The English cases of *Bennett* v. *Ogston*[1] and *Hillerns and Fowler* v. *Murray*[2] were relied upon by Sir Jamshedji Kanga. They must be approached with the caution enjoined by the Judicial Committee in numerous cases to the effect that the Indian Act and the English statutes are not in *pari materia*. However, as stated by Lord Greer in the case of *Hillerns and Fowler* v. *Murray*[2], the reason why the outstanding fees of a professional man, which come in after the discontinuance of the profession, are not taxable in England is "by reason of the technical application of the provision of the taxing Acts." Although the scheme of the English and the Indian Acts is very different, the technical satisfaction of tax antecedently, in my opinion, is equally applicable.

Lastly, the question of the relevant year was adumbrated, that is to say, whether the year, to which the termination of the profession is relevant, is the accounting year or the assessment year. In *Indian Iron & Steel Co., Ltd.* v. *Commissioner of Income-tax, Bengal*[3], Lord Porter in delivering the judgment of the Board states that in the case of a succession to a business "if ......company A sold its business to company B in the first of the two years, apart from the provisions of Section 26 (2), the former company could not be assessed and would not be liable for any profits it then made, because it would not be carrying on the business in the next year for which in the normal course the assessment would be made and in respect of which tax would be due......."

Except, therefore, for the special provisions found in sub-section 26 (2), which deals with cases of succession, the relevant year is the assessment year and not the accounting year. In my opinion, in the case of the discontinuance of a business, profession or vocation the same result would follow but for the provisions of Section 25.

Accordingly, for the reasons stated above, it is my opinion that the question referred to us ought to be answered in the negative.

KANIA, J.—I had an opportunity of reading the judgment just delivered by the learned Chief Justice. After giving it anxious consideration I regret I am unable to agree with his view.

(1) (1930) 15 Tax Cas. 374.
(2) (1932) 17 Tax Cas. 77.
(3) (1943) 11 I.T.R. 328, p. 336.

This is a reference made under Section 66 (2) of the Indian Income-tax Act, 1922, by the Commissioner. The relevant facts are that the assessee was the sole proprietor of a business run in the name of "Kamdar Karyalaya" and was also carrying on the profession of a consulting civil engineer in Bombay. The business of "Kamdar Karyalaya" was converted into a limited company, styled Kamdar Ltd., on February 15, 1938, and the assessee was appointed the "managing member" of the company. The business of "Kamdar Karyalaya" was transferred to the limited company. The question before us does not relate to that part of the transaction.

After February 15, 1938, the assessee did not carry on the profession of a consulting civil engineer as before. The accounting year of the assessee was 1938. In respect of his professional earnings he kept accounts on the basis of receipts and his income of the previous years was computed on that footing. In respect of his income in 1938, the assessee contended that as he had ceased to carry on the profession of a consulting civil engineer in 1938 he was not liable to be assessed in respect of his fees for that year. In the alternative, it was urged that, in any event, after February 15, 1938, such outstanding (professional) fees as were received by him were not income, because he had ceased to carry on the profession of a consulting civil engineer and the recoveries were debts. It is common ground that these receipts were fees to which the assessee became entitled because of the practice of profession before February 15, 1938. It was contended on his behalf that where the "carrying on of profession" ceased, the source had come to an end and therefore there could be no income in respect of the profession thereafter. In support of this contention counsel relied on the following observations of Rowlatt, J., in *Bennett* v. *Ogston*[1] :—

"When a trader or a follower of a profession or vocation dies or goes out of business...and there remain to be collected sums owing for goods supplied during the existence of the business or for services rendered by the professional man during the course of his life or his business, there is no question of assessing those receipts to income-tax; they are the receipts of the business while it lasted, they are arrears of that business, they represent money which was earned during the life of the business and are taken to be covered by the assessment made during the life of the business, whether that assessment was made on the basis of bookings or on the basis of receipts."

The same learned Judge in *Hillerns and Fowler* v. *Murray*[2] again observed as follows :—

(1) (1930) 15 Tax Cas. 374, p. 378.
(2) (1932) 17 Tax Cas. 77, p. 81.

"Under those circumstances, the question is whether, during this year of assessment ending April, 1927, they were trading. If they were not trading they could not be assessed any more than a retired professional man can be assessed if after he retires he receives fees from clients or patients according to what his profession is—and, if you like, also pays arrears of rent for the premises in which he formerly carried on his business."

Counsel for the assessee very strongly relied on *Commissioner of Income-tax* v. *Shaw Wallace & Co.*[1] In that case the respondent company carried on business at Calcutta as merchants and agents of various companies and had branch offices in different parts of India. For a number of years prior to 1928 they acted as distributing agents in India of the Burma Oil Co., Ltd., and the Anglo-Persian Oil Co., Ltd., but had no formal agreements with either company. In or about 1927 the two companies joined and decided to make other arrangements for distribution of their products. The respondents' agency with the Burma Oil Co. was accordingly terminated on December 31, 1927, and that of the Anglo-Persian Co. on June 30, 1928. Some time in the first half of 1928 the Burma Oil Co. paid to the respondents Rs. 12,00,000 "as full compensation for cessation of the agency" and in August of the same year the Anglo-Persian Oil Co. paid to them a sum of Rs. 3,25,000 as "compensation for the loss of your office as agents of the company." These expressions were accepted as correctly describing the nature of the transactions. On behalf of the Commissioner it was sought to be argued that these payments were income in 1928 and liable to be taxed. The contention was negatived by the High Court at Calcutta and also by the Privy Council. Sir George Lowndes in his judgment observed as follows (pages 212-214):—

"The object of the Indian Act is to tax 'income,' a term which it does not define. It is expanded, no doubt, into 'income, profits and gains,' but the expansion is more a matter of words than of substance. Income, their Lordships think, in this Act connotes a periodical monetary return 'coming in' with some sort of regularity, or expected regularity, from definite sources. The source is not necessarily one which is expected to be continuously productive, but it must be one whose object is the production of a definite return, excluding anything in the nature of a mere windfall. Thus income has been likened pictorially to the fruit of a tree, or the crop of a field...

"The claim of the taxing authorities is that the sum in question is chargeable under head (iv) business. By Section 2, sub-section (4), business 'includes any trade, commerce or manufacture, or any adventure or concern in the nature of trade, commerce or manufacture,'

(1) (1932) 59 I. A. 206.

The words used are no doubt wide, but underlying each of them is the fundamental idea of the continuous exercise of an activity. Under Section 10, the tax is to be payable by an assessee under the head business 'in respect of the profits or gains of any business *carried on by him.*' Again, their Lordships think, the same central idea: the words italicised are an essential constituent of that which is to produce the taxable income: it is to be the profit earned by a process of production. And this is borne out by the provision for allowances which follows...

"Following the line of reasoning above indicated, the sums which the appellant seeks to charge can, in their Lordships' opinion, only be taxable if they are the produce, or the result, of carrying on the agencies of the oil companies in the year in which they were received by the respondents. But when once it is admitted that they were sums received, not for carrying on this business, but as some sort of solatium for its compulsory cessation, the answer seems fairly plain."

Towards the close of the judgment it was observed as follows (page 215):—

"Their Lordships will only add that the reasoning of this judgment would apply equally if the appellant based his claim on head (vi) 'other sources' and the corresponding provisions of Section 12."

Relying on these observations it was argued that in order to constitute "income" the sum must flow or grow out of a source in existence in the accounting year. In this connection the provisions of Section 24 of the Act were also relied upon. It was pointed out that unless the business was carried on in the accounting year, the loss of the previous year, which was carried over and permitted to be set off, could not be set off. Section 24 permitted such set-off only when the same business was continued. It was urged that while Sections 3 and 4 were charging sections, Chapter III commencing with Section 6 dealt with "taxable income." Under Section 6 it was provided that income shall be shown under five heads and the fourth head was "profits and gains of business, profession or vocation." Income under that head was dealt with in Section 10. That runs as follows:—

"The tax shall be payable by an assessee under the head 'profits and gains of business, profession or vocation' in respect of the profits or gains of any business, profession or vocation carried on by him."

It was urged that the very idea of income postulates the existence of source in the year in which it is taxed. Unless the source existed it could not be stated that it was income of the business or profession carried on by the assessee. Contending that the allowances provided by Section 10 were all in respect of a source which existed in the accounting year, it was argued that if no machinery was provided for

allowances to be given on the footing of receipts, it was a strong argument for holding that the amount received after a source had ceased to produce further income was not taxable.

On the construction of the Indian Income-tax Act it was contended that unless the income fell under any of the heads mentioned in Sections 6 to 12 it was not taxable income. It was argued that Section 6 and not Section 4 was the charging section and the heading of Chapter III and the words of Section 6 were relied upon in this connection. Counsel also relied on *Probhat Chandra Barua* v. *The King-Emperor*[1], where at page 238 it was observed :—

" Although Chapter I is entitled ' Charge of Income-tax,' the real charging section would appear to be Section 6, which occurs in Chapter III."

It was strenuously urged that the governing section was Section 6 read with Section 10 and not Section 4. It was contended that the scheme of the Indian Act was to tax all income on the accrual basis, and in respect of income from business and other sources although the tax was on that basis, for computation the Act had permitted different methods under Section 13. That, however, was only for computation. The result was that once the income of the "previous year" was taxed and the source ceased at the end of the year, there remained nothing to tax in the next year when the source did not exist. In respect of Section 4 (1) (a) it was contended that the same applied to receipts by non-residents only and not to all persons. All were taxed alike on accrual basis as under the English Income Tax Act of 1918.

Against this it was contended on behalf of the Commissioner that the English law was different in material respects from the Indian Income-tax Act and observations found in the English cases should not be considered relevant. It was urged that Section 4 was the charging section and the only relevant question was whether the amount could be included in the expression "total income" under that section. Once an amount was classified as "income," it did not alter its character because it was received later. As regards the allowance and set-off permitted under Sections 10 and 24 respectively it was argued that the same were permitted as provided in those sections, and Section 10 (2) was wide enough to cover expenditure laid out for business or profession even though it had ceased to be carried on in the accounting year.

Our attention has not been drawn to any decision on the construction of Section 4 after its amendment in 1939. Therefore it is desirable first to look at the provisions of the Income-tax Act in force in

(1) (1930) 57 I.A. 228.

the assessment year. It is common ground that the Act as amended in 1939 is applicable to the case before us. In order to appreciate the rival contentions of the parties it is necessary to notice the relevant provisions of the Act of 1922 and consider the same with the amended provisions of the Act of 1939. This is material because several decisions of the Privy Council which have been relied on were pronounced on the wording of the sections of the Act of 1922. The Act of 1922 was an Act to consolidate and amend the law relating to income-tax and super-tax. In Section 2 (15) the expression 'total income' was defined as follows: "'Total income' means total amount of income, profits and gains from all sources to which this Act applies computed in the manner laid down in Section 16." Section 3 provided that the rate applicable to the total income of the assessee would be the rate prescribed in the Act of the Central Legislature from time to time. Section 4, sub-sections (1) and (2), were in these terms:—

"4. (1) Save as hereinafter provided, this Act shall apply to all income, profits or gains as described or comprised in Section 6, from whatever source derived, accruing, or arising, or received in British India, or deemed under the provisions of this Act to accrue, or arise, or to be received in British India.

(2) Income, profits and gains accruing or arising without British India to a person resident in British India shall, if they are received in or brought into British India, be deemed to have accrued or arisen in British India and to be income, profits and gains of the year in which they are so received or brought, notwithstanding the fact that they did not so accrue or arise in that year."

In the remaining portion of Section 4 provision was made for exemption from tax of certain kinds of income, *e.g.*, agricultural income, income arising or accruing in a State of India, charitable income, income of local authorities and several others. Chapter III was headed 'Taxable Income' and Section 6 was in these terms:—

"6. Save as otherwise provided by this Act, the following heads of income, profits and gains shall be chargeable to income-tax in the manner hereinafter appearing, namely:—

(*i*) Salaries.
(*ii*) Interest on securities.
(*iii*) Property.
(*iv*) Business.
(*v*) Professional earnings.
(*vi*) Other sources."

Section 10, sub-section (1), provided as follows:—

"The tax shall be payable by an assessee under the head 'Business' in respect of the profits or gains of any business carried on by him."

Sub-section (2) provided: " Such profits or gains shall be computed after making the following allowances namely :...... "

Section 11, sub-section (1), provided as follows:—

" The tax shall be payable by an assessee under the head " Professional earnings " in respect of the profits or gains of any profession or vocation followed by him."

Sub-section (2) provided:—

" Such profits or gains shall be computed after making the following allowances, namely:—(i) any expenditure (not being in the nature of capital expenditure) incurred solely for the purposes of such profession or vocation, and not being personal expenses of the assessee..."

Section 12, sub-section (1), provided as follows:—

" The tax shall be payable by an assessee under the head ' Other sources ' in respect of income, profits and gains of every kind and from every source to which this Act applies (if not included under any of the preceding heads)."

Sub-section (2) provided:—

" Such income, profits and gains shall be computed after making allowances for any expenditure (not being in the nature of capital expenditure) incurred solely for the purpose of making or earning such income, profits or gains, provided that no allowance shall be made on account of any personal expenses of the assessee."

The relevant part of Section 13 was: Income, profits and gains shall be computed for the purpose of Sections 10, 11 and 12 in accordance with the method of accounting regularly employed by the assessee. Section 16 dealt with certain general exceptions which are not material. The rest of the sections are not material to the present discussion.

In the amended Act of 1939 " Total income " is defined in Section 2 (15) in these terms: " ' Total income ' means total amount of income, profits and gains referred to in sub-section (1) of Section 4 computed in the manner laid down in this Act." For the present discussion there was no material change in Section 3. Section 4 was recast and the material portions run as follows:—

" 4. (1) Subject to the provisions of this Act, the total income of any previous year of any person includes all income, profits and gains from whatever source derived which—

(*a*) are received or are deemed to be received in British India in such year by or on behalf of such person, or

(*b*) if such person is resident in British India during such year,—

(*i*) accrue or arise or are deemed to accrue or arise to him in British India during such year, or

(*ii*) accrue or arise to him without British India during such year, or

(*iii*) having accrued or arisen to him without British India before the beginning of such year and after the 1st day of April, 1933, are brought into or received in British India by him during such year, or

(*c*) if such person is not resident in British India during such year, accrue or arise or are deemed to accrue or arise to him in British India during such year."

Then follow various provisions for exemptions of different kinds of income. Section 6 of the amended Act is in the same terms as before except that the fourth head is " profits and gains of business, profession or vocation " all put together and head 5 is omitted. Section 10 was also correspondingly amended and runs as follows :—

" 10. (1) The tax shall be payable by an assessee under the head ' profits and gains of business, profession or vocation ' in respect of the profits or gains of any business, profession or vocation carried on by him.

(2) Such profits or gains shall be computed after making the following allowances, namely :—

* * * *

(*xii*) any expenditure (not being in the nature of capital expenditure or personal expenses of the assessee) laid out or expended wholly and exclusively for the purpose of such business, profession or vocation ; "

Section 11 is deleted by the Act of 1939. Section 12 remains unchanged. Section 13 remains as before, after omitting all reference to Section 11.

The whole contention of the assessee is based on the argument that as the source of income, *viz.*, the practice of profession had ceased in the year 1938, the receipts after February 15 were not income and not liable to tax. This argument cannot be accepted because it cannot be stated that throughout that year the source was not in existence. It is admitted that the assessee ceased to act as a consulting architect from February 15, 1938. Therefore, the utmost which could be urged is that the source ceased to exist on February 15, 1938.

The question then arises if in respect of the fees earned for work done and completed in 1937 and up to February 15, 1938, there is a difference, if the receipt was on or before February 14 or after February 16. The argument urged by the assessee would make a difference in the amount liable to tax, according to the dates of receipt in the accounting year.

The scheme of the amended Act of 1939 appears to be this: Chapter I, in which Sections 3 and 4 are found, is headed, "Charge of Income-tax." As the words "total income" on which the charge has to be made occur in Section 3, it is necessary first to find out what that expression means under the Act. The second question is whether it is assessable in the year in question, because the law considers it the assessee's income of the previous year. The definition of total income found in Section 2 (15) shows that in respect of the amount to be included in the expression two things are essential: (1) The income, profits and gains should be referred to in Section 4, sub-section (1); and (2) it should be computed in the manner laid down in the Act. This is an artificial definition for the purpose of the Act. The main body of sub-section (1) of Section 4 provides that the total income of any previous year "includes" *all* income, profits and gains from whatever source derived. Having ascertained that it is such income, and the receipt is not of any other class, the next thing is to turn to clauses (*a*), (*b*) and (*c*) of the sub-section. The clauses show, (*a*) that it should be received or deemed to be received in British India in such year, *or* (*b*) if such person is resident in British India, it accrues or arises or is deemed to accrue or arise to him under clauses (*i*), (*ii*) and (*iii*) in such year, *or* (*c*) if such person is not resident, it has accrued or arisen to him in British India during such year. It cannot be disputed that the words used in Section 4 (1) (*a*) relate to the first receipt after the accrual of income. Once it is received by the party entitled to it, in respect of any subsequent dealing with the said amount, it cannot be said to be "received" as income on that occasion. Section 4 (1) (*b*) is not limited only to income accrued to the person in the previous year. Clause (*iii*) covers income received in foreign country between April 1, 1934, and the beginning of the previous year, but brought into British India in the previous year. Moreover, the words in the main body of the section do not refer to any period during which the income, profits or gains have been derived. There appears no justification for reading "in the previous year" in the main body of the section. The limitation of time is found in appropriate words in each of the clauses. According to Section 4 therefore two questions arise: (1) whether the amount in question is income, profits and gains, from whatever sources derived; and (2) whether such income falls within the words found in sub-section (*a*), (*b*) or (*c*). If the answer to these questions is in the affirmative, the next process is to ascertain if such income is excluded under Section 4 (3) from tax. This is material because the heading of this section is "Applicability of the Act." Section 4 itself excludes certain income, like agricultural income or

income of charitable trusts from taxation. If it was so excluded, the same ceased to be income for the Act, and no computation is necessary to be made. If the amount passes these tests, it becomes income referred to in Section 4 (1).

According to Section 2 (15), one has next to compute the income in the manner laid down in other parts of the Act. Section 6 is in Chapter III which is headed "Taxable Income." That section enacts that the following heads of income, profits and gains shall be chargeable to tax in the manner thereafter appearing. It is clear, therefore, that Section 6 does not attempt to define income or prescribe limitations on income. It only sets out the heads under which income, which has been referred to in Section 4 (1), is chargeable. The heads which are particularly dealt with in Sections 7, 8, 9, 10 and 12 do not also attempt to define the conditions under which the income is charged. They prescribe the manner in which the charge, under each head, has to be made. That appears to me to be the scheme, because in respect of each head a different method of computation in respect of allowances is prescribed. If the Income-tax Act contained only the provisions found in Sections 2 (15), 3 and 4, the gross income would be liable to tax, because there would be no provision for any deductions for expenses incurred in order to earn the income. Bearing that in mind the wording of Sections 6 and 12 should be particularly noticed. Having arrived at the total income liable to be taxed under Section 4 the scheme of the Act is not to tax such gross income, but to tax what is legitimately considered his income, after allowing for expenses incurred to earn the gross income. Therefore, the total of the gross receipts is not made taxable as one item. Certain heads, covering particular sources, are specified in Section 6 and the provision is that "the heads" mentioned therein "shall be chargeable to income-tax in the manner" thereafter appearing. The section begins with the words "Save as otherwise provided by this Act" so as not to exclude the operation of any other section permitting a deduction. The result is that Section 6 specifies five heads and provides that under those heads income shall be chargeable in the manner appearing thereafter. The last head is necessarily made a wide residuary head so as to cover and include everything which had not fallen under any of the other heads but was included in the expression "total income." Because of the generality of that head the deductions permissible under Section 12 are necessarily generally worded, so as to achieve the result of finding out the net income of the assessee under that head. In my opinion, Sections 6 to 13 are thus not the charging sections but are inserted in the Act for computation of the net income of the assessee.

This construction is in accord with the view that under the Act income, and not several incomes, is taxed. Indeed this is the view taken by Lord Russell in *Probhat Chandra Barua* v. *The King-Emperor*[1], where he stated that the scheme of the Act is not to tax the gross receipts and the different heads specified in Section 6 are for the purpose of arriving at the taxable balance after the necessary deductions and allowances are made from gross receipts. In *Commissioner of Income-tax, Bombay Presidency and Aden* v. *Chunilal B. Mehta*[2], Sir George Rankin stated that the effect of Section 6 was to classify the profits and gains under different heads for the purpose of providing appropriate rules for computing the amount of tax. He further stated (even when there was an express reference in Section 4 (1) to Section 6 in the Act before its amendment in 1939) that Section 6 is intended as describing different kinds of profit and that if the condition "accruing, arising or received in British India, etc." is satisfied by the profits, they will not escape the tax by reason of any quality or circumstance of the source.

Again Sections 7 to 12 divide themselves into two parts. Sections 7, 8 and 9 provide for charging tax, irrespective of the manner in which the assessee keeps his books. Salaries have to be charged as earned, whether the same are received or not by the assessee in the accounting year. Interest on securities under Section 8 is to be charged to tax if it is receivable by the assessee, *i.e.*, irrespective of the question whether it is received or not. Under Section 9 the income from property is charged on the *bona fide* annual letting value of the property of which the assessee is the owner, irrespective of the question whether such value as computed by Section 9 (2) is received or not. This must be computed subject to the limitations and provisos found in that section. The important fact to remember is that the method of accounting adopted by the assessee is immaterial for these sections. Sections 10 and 12 stand on a different footing. In addition to the manner in which the income is to be computed and the deductions allowed under each of those sections, Section 13 provides that the computation shall be in accordance with the method of accounting regularly employed by the assessee, unless the Income-tax Officer in any individual case finds that the method so adopted does not disclose the true income of the assessee. Except for that contingency Section 13 requires the department to compute the income according to the method of accounting regularly adopted by the assessee.

The Income-tax Act has never attempted to define the word "income." The result is that at different times Judges have described

(1) (1930) 57 I.A. 228, at p. 240. (2) (1938) 65 I.A. 332, at p. 347 ; 6 I.T.R. 521.

the word in different language. Apart from the definition of "income," the scheme of the Act therefore is clear. The arguments based on deductions and set-off found in Section 24 do not for this purpose affect the material question. Once the income is found to be referred to in Section 4 (1), and is computed in the manner laid down in the Act, the same is taxable under Section 3. The amendments made by the omission of Section 11 should be particularly noticed. In the body of Section 10 the words "profession or vocation" are added while in sub-section (2), where deductions are provided, clause (*xii*)—which was the only clause for deductions under old Section 11—is bodily included, without any change. The result is that a general head (*xii*) of allowances in respect of business, which did not exist before, is now included in Section 10.

The contention that Section 10 is an independent section or that it controls in any way the income referred to in Section 4, sub-section (1), is, in my opinion, unsound. I concede that the two sections have to be read together, but the process is to approach Section 4 (1) first, and, thereafter, for the purpose of computation [as provided in the definition in Section 2 (15)], the other sections of the Act have to be referred to. If the department seeks to bring a portion of income [as referred to in Section 4 (1)] to charge under the head "Business, etc.," the same should be computed according to the rules found in Section 10 read along with Section 13. The amount of the total income referred to in Section 4 (1) having been first ascertained, the department has to allocate it under the different heads mentioned in Section 6, and if it does not fall under any of the specific heads 1 to 4, it must go under the general head "Other sources," because the scheme clearly is that all income referred to in Section 4 (1) must come for charge under one or the other of the heads mentioned in Section 6 and dealt with in Sections 7 to 12.

The Judicial Committee of the Privy Council had occasion to examine the scheme of the Indian Income-tax Act of 1922, and consider the meaning of the word "income" before the Act was amended in 1939. I shall therefore next consider those decisions, only with a view to ascertain their Lordships' views about the scheme of the Act. As the word "income" is not defined in the amending Act also, those observations still hold good. In *Probhat Chandra Barua* v. *The King-Emperor*[1], the question arose about the assessment to tax the income of a zamindari. In the course of its judgment the Board considered the scheme of the Act of 1922 and noticed that it was an Act to consolidate and amend the law relating to tax. Sections 3 and 4 in Chapter I

(1) (1930) 57 I.A. 228.

which was headed " Charge of Income-tax " were considered and it was observed "although Chapter I is entitled ' Charge of Income-tax,' the real charging section would appear to be Section 6, which occurs in Chapter III " which was intituled ' Taxable Income, ' and was composed of Sections 6 to 17 inclusive. The Board next considered the six sections following Section 6 and pointed out that they dealt with greater particularity the items in respect of which the tax was payable by the assessee under the particular head, and those sections gave details of allowances and exemptions with regard to different heads. It next considered that income of zamindari would not be chargeable under the head " Property " because that head was confined to the annual letting value of buildings or lands appertaining thereto. It therefore held that Section 12 covered the case. The words of Section 12 are in respect of income, profits and gains of every kind and from every source to which this Act applies, if not included in any of the preceding heads. Their Lordships observed as follows (page 239) :—

" . . . These words appear to their Lordships clear and emphatic and expressly framed so as to make the sixth head mentioned in Section 6 describe a true residuary group embracing within it all sources of income, profits and gains provided the Act applies to them, *i.e.*, provided that they accrue or arise or are received in British India or are deemed to accrue or arise or to be received in British India, as provided by Section 4, sub-section (1), and are not exempted by virtue of Section 4, sub-section (3)."

According to these observations it is therefore clear that all income which was covered by Section 4 (1), and was not exempted by virtue of Section 4 (3), was to be charged under one or the other of the heads separately mentioned in Section 6 ; and if it was found not to fall within the words of a particular head, it was embraced by the residuary group, *viz.*, the last head, " Other sources." The observation, that although Chapter I is intituled " Charge of Income-tax " the real charging section would appear to be Section 6 which occurred in Chapter III, in my opinion, was due to the express reference to Section 6 in Section 4 (1) of the Act of 1922. The income, profits and gains, to which that Act applied, therefore, were as described or comprised in Section 6. Those words are now omitted from Section 4 (1). In my opinion, therefore, those observations do not apply to Section 4 (1) under the present Act. Two vital changes are made in this connection by the Amending Act of 1939 : (1) All reference to Section 6 is omitted in Section 4, and (2) in the definition of Section 2 (15) there is an express reference to Section 4 (1). It should

also be noticed that the division of Section 4 (1) into three clauses is new and makes a vital change in answering the first question, " What income is to be included in the expression 'Total income' in Section 3 ? " This decision therefore supports the view that to ascertain the total income the first approach is to Section 4 (1), next to Section 4 (3) and then to allocate it under one or other of the heads described in Section 6.

The argument advanced on behalf of the assessee that this construction will result in a tax on gross receipts was also disposed of at page 240 in the following terms :—

" The tax is upon 'income, profits and gains.' It is not a tax on gross receipts. With this fact in view, each section which deals with one of the first five 'heads' specified in Section 6 contains, where proper, specific provisions for the necessary deductions and allowances to be made for the purpose of arriving at the taxable balance. Section 12, which deals with the general residuary group, is necessarily framed in general terms and authorises the allowance of any " expenditure (not being in the nature of capital expenditure) incurred solely for the purpose of making or earning such income, profits or gains."

It is therefore clear that the scheme of the Act is never to charge tax on gross receipts but all proper deductions, as prescribed by the Act, must be made in computing the total.

In *Commissioner of Income-tax* v. *Shaw Wallace & Co.*[1], the Privy Council considered the meaning of the word " income " in connection with business. The facts of that case and the definition of " income " given therein have been set out in the early part of this judgment. The amounts in that case were held not liable to tax because they were not the produce or the result of carrying on agencies but they were received as solatium for its compulsory cessation. It must be conceded that, if an amount is received, not as a fruit of the business, but as compensation for cutting off the tree, it cannot be called income in any sense of the word. It is on that ground that the Court rejected the contention of the taxing authority. The emphasis on the words " carried on " in Section 10 was to point out that the amount was not received for carrying on, but for *not* carrying on the business. To argue that the Privy Council had held in that case that unless the source was in existence in the year of assessment it should not be considered income at all, is a misreading of the judgment. The case is not an authority and does not purport to state that if the payments were in respect of their commission earned when the agencies subsisted, they were not income under Section 10 because the receipts were after the termination of the agencies. Every case is an authority only

(1) (1932) 59 I.A. 206; 59 Cal. 1343.

for the proposition it lays down. The Board was not concerned in that case with the question, "If the receipts were income of the agencies would it make any difference if they were received later on?" In my opinion that case while defining pictorially the word "income" does not lay down the proposition urged by the assessee.

In *Gopal Saran Narain Singh* v. *Commissioner of Income-tax, Bihar and Orissa*[1], the Board had to consider the meaning of the word "income" and the application of Sections 4 and 12 of the Act. The facts shortly put were these: The assessee who owned a nine annas share in an estate conveyed the greater portion of that estate to X who owned the remaining seven annas. The consideration of the transfer was (1) payment of the assessee's debts amounting to Rs. 10,26,937, (2) a cash payment of Rs. 4,73,063, and (3) an annual payment of Rs. 2,40,000, to the assessee for life. The contention which was ultimately argued before the Privy Council was whether the annual payment of Rs. 2,40,000 was liable to tax as income. In delivering judgment Lord Russell at page 242 observed as follows:—

"The word 'income' is not limited by the words 'profits' and 'gains.' Anything which can properly be described as income, is taxable under the Act unless expressly exempted. In their Lordships' view the life annuity in the present case is 'income' within the words used in the judgment of this Board which was delivered in the case of *Commissioner of Income-tax* v. *Shaw Wallace & Co.*[2]"

According to that judgment therefore the Court had first to find whether the amount in question was "income" and if it was not exempted under the Act, it was liable to tax. The Board approved of the definition of the word "income" given in *Shaw Wallace's case*[2].

In *Commissioner of Income-tax, Bombay Presidency and Aden* v. *Chunilal B. Mehta*[3], the Board had occasion to consider again the applicability of Sections 4 and 6 in the matter of taxing a particular amount. The question was whether the amount was covered by the words "accruing or arising or received in British India." Sir George Rankin observed (page 347):—

"They will first deal with the argument, based on Sections 4 and 6, that the respondent's business is the source of the profits, and that the sections require that the situation of the source should determine the place where the profits arise. This, in their Lordships' view, is a straining of the sections. The effect of Section 6 is to classify profits and gains under different heads for the purpose of providing for each appropriate rules for computing the amount; its language is 'shall be chargeable...in the manner hereinafter appearing.' One of the heads

(1) (1935) 3 I.T.R. 237; 37 Bom. L.R. 817.
(2) (1932) 59 I.A. 206; 59 Cal. 1343.
(3) (1938) 65 I.A. 332; 6 I.T.R. 521, at p. 529.

is 'Business,' which as a head of income stands alongside Salaries, Interest on securities, Professional earnings, and Other sources. True, the classification of income is according to the character of the source, and it has been held that 'income, profits and gains' as distinct from casual receipts and from other forms of receipt or enrichment, involve the idea of a periodical money return from a definite source...But the list of 'heads' in Section 6 is a list of sources not in the sense of attributing the income to one property rather than another, one business rather than another, but only in the sense of attributing it to property as distinct from employment, or business as distinct from investment. Sections 4 and 6, taken together, say of business profits that *they are taxable on certain conditions stated in Section 4 and in a manner to be laid down in a later section*...What is to be learnt from an examination of the language of sub-section (1) of Section 4...is that Section 6 is intended as describing different kinds of profit and that if the condition 'accruing, or arising or received in British India etc.,' is satisfied by the profits, they will not escape by reason of any quality or circumstance of the source....There is every presumption that in such a section in an Indian Act the legislature intends the exact language of the section to be the test of liability. To answer the question, 'Do these profits accrue or arise in British India?' by asking another, 'What in the sense of Section 6 is the source of these profits, and is it situate in British India?' is to divert attention from that to which the statute points and to devote attention to what it discards...However that may be, the profits of each particular business are to be computed wherever and by whomsoever the business is carried on, but only on condition that they are profits 'accruing, or arising or received in British India'..." (The italics are mine).

These observations clearly emphasise that while Section 6 is intended as describing different kinds of profits, reference must be made to the words in Section 4 to ascertain what is income under the Act.

In *Kamakshya Narain Singh* v. *Commissioner of Income-tax*[1], the Board had to consider whether royalty paid in respect of a mining lease under certain conditions was liable to tax. The contention that profits and gains of business only were liable to tax and the word "income" was limited by those words was rejected by approving the following observations of Lord Russell in *Gopal Saran Narain Singh's case*[2]: "The word 'income' is not limited by the words 'profits and gains.' Anything which can be properly described as 'income' is taxable under the Act unless expressly exempted." The Board did not appear impressed by the pictorial definition of "income" given

(1) (1943) 11 I.T.R. 513. (2) (1935) 3 I.T.R. 237.

in *Shaw Wallace's case*[1]. Lord Wright in delivering judgment of the Board stated (page 522) :—

"But it is clear that such picturesque similes cannot be used to limit the true character of income in general, and particularly when it is constituted by mining rent or royalties."

The Board held that royalties were income within the meaning of the Act, whatever be the exact definition of the word. It was then observed as follows (page 523) :—

"Income is not necessarily the recurrent return from a definite source, though it is generally of that character. Income, again, may consist of a series of separate receipts, as it generally does in the case of professional earnings. The multiplicity of forms which 'income' may assume is beyond enumeration."

None of these decisions in my view support the contention that the source must be in existence at the time of receipt. In fact Section 4 (1) (b) (iii) shows that income may have accrued in England in 1934, and although the source may have ceased in 1938, if the same was brought in British India in 1940, it was taxable. If the existence of the source is immaterial for this sub-clause, I see no reason why it should be considered material for the construction of the words in the main part of Section 4 (1). The opening words of Section 4 (1) "Subject to the provisions of this Act.........." are inserted only to find out if any income, which is referred to in Section 4 (1), is exempted under the same section or another section of the Act. As in my opinion Sections 6 to 12 are not sections defining or limiting the word "income," the above quoted words in Section 4 do not support the contention of the assessee. The absence of all reference to Section 6 in Section 4, and the words used in Section 6, make Sections 7 to 12 as laying down now only the manner in which the income (which has been referred to in Section 4) has to be charged, according to the rules of computation relating to each individual head found in the said sections. Having regard to the scheme of the Act the questions to be considered are: (1) Whether it is income referred to in Section 4 (1). (2) If so, whether it is exempted under Section 4 or any other section of the Act. The next step is to divide the income so arrived at under the heads mentioned in Section 6 and compute the same in the manner laid down in those sections. In respect of "business" and "other sources" the provisions contained in Section 13 have also to be applied. The result is the "total income" on which tax is to be levied as prescribed by Section 3 of the Act. This method of approach does not leave any difficulty in the plain reading of the Act.

(1) (1932) 59 I.A. 206 ; 59 Cal. 1343.

Counsel for the assessee also relied on *B. C. G. A. (Punjab), Ltd.* v. *Commissioner of Income-tax, Punjab*[1]. In that case the assessee had kept his accounts on the mercantile system under Section 13. A question arose in respect of certain debts which had become time-barred. It was contended that they had become time-barred in the year in question and therefore became bad debts for which the assessee claimed deductions. The taxing authorities rejected the contention on the ground that they had become bad debts before the assessment year and the Court held that they had no power to interfere with the finding. In the course of his judgment Din Mohammad, J., observed as follows (page 304) :—

"This being so, the question arises whether the assessee can claim any relief on account of those losses, the business having been long discontinued before the year of account. The answer is clearly in the negative. In *South Indian Industrials Ltd.* v. *Commissioner of Income-tax*[2], in a case where the assessee had carried on several separate businesses before, but in the account year some of those businesses had closed, a Special Bench of the Madras High Court held that the assessee could not set off the losses of the discontinued businesses against the profits of the current businesses, inasmuch as Section 10 of the Income-tax Act dealt with businesses that were being carried on and not with businesses which had ceased to exist, and further that the losses were capital losses and not revenue losses."

It was emphasised that in order to claim a set-off the condition precedent was that both businesses should be alive during the current year. Dead business's losses cannot be set off against living business's gains. These observations must be read with the facts of the case. If it is appreciated that the accounts are kept on mercantile basis, the question of receipts does not come in ; at the end of each year the total profits or loss on the basis of accrual are assessed and taxed. During the last year of business, when it was closed, all its profits and losses computed in the manner permitted by the Act were assessed and taxed. Thereafter, there can remain nothing to accrue or to be taxed in respect of that business. The contention is unsound when the computation is on the receipt basis, and, in my opinion, those observations are inapplicable when the mercantile basis was not the method of accounting.

Counsel for the assessee strongly relied on the two English cases mentioned at the commencement of the judgment. In *Bennett* v. *Ogston*[3] the facts were these: A person doing money-lending business died. During his lifetime he had taken from his debtors bonds, which were

(1) (1937) 5 I.T.R. 279.
(3) (1930) 15 Tax Cas. 374.
(2) (1935) 58 Mad. 433 ; 3 I.T.R. 11.

payable at stated intervals, and which included certain portions of the loan and interest thereon. After the death of the money-lender certain bonds were discharged by the debtors by payment. It was argued on behalf of the estate of the deceased that this was not income as the trade had come to an end. The contention was rejected because it was pointed out that the repayment was of interest on capital which had remained advanced even after the death of the trader, and therefore was income. In discussing the liability of such receipts to tax Rowlatt, J., observed that the source must be in existence at the time of the receipt of the income, and if the trade or profession had ceased, the receipts were not chargeable to tax. In *Hillerns and Fowler* v. *Murray*[1], on facts, it was found that the firm was trading when the amount was received, and, therefore, the question whether the income was received after the source had come to an end did not arise. In discussing the question of liability if the trade had stopped, Rowlatt, J., made observations similar to what he had made in the former case. In my opinion those cases are not relevant for the present discussion. The scheme of the English Act is entirely different from the scheme of the Indian Act. Under the English Act the tax is on the income of the assessment year, *i.e.*, the current year's income. As some or a large portion of the year is still to run at the time of assessment, the previous year's or the average income of certain years is taken as a measure; but the tax is still on the current year's income. The result is that the basis of taxation is accrual and not receipts, as contemplated by Section 4 (1) (a). The opening words of Schedule D of the English Act show that the charge is on the accrual basis and not on the basis of receipts at all. A comparison of the two Acts shows that there is nothing like Sections 20, 30 and 31 of the English Act of 1926 in the Indian Income-tax Act.

In the matter of assessment of *Behari Lal Mullick, In re*[2], the assessee was the owner of two house properties, one of which was mortgaged. Income during the "previous year" was received from the property but in the year of assessment the property was sold by the mortgagee. Relying on the principles of *Brown* v. *National Provident Institution*: *Ogston* v. *Provident Mutual Life Association*[3] and *Whelan* v. *Henning*[4], it was contended that as the assessee had no income from the property in the year of assessment no income-tax was due from him, notwithstanding that in the previous year he derived income from that source. The next question of law on which the Court was asked to give its opinion was on the basis that while in

(1) (1932) 17 Tax Cas. 77.
(2) (1927) 54 Cal. 630.
(3) [1921] 2 A.C. 222.
(4) [1926] A.C. 293.

the "previous year" the assessee received an income from ground-rent, he had, in the year of assessment, derived no income from that source. The Court held that the Indian Act of 1918 was framed on the model of the English Act. It was pointed out that under the English Act the assessment in any particular year was made on the income which the Legislature deemed the assessee to have received in the year of assessment. The Legislature imputed statutory income to the assessee for computation of income for the year of assessment. A reference to the previous year's income, under the English Act, was made only for the purpose of measurement and for computation of tax for the year of assessment. The observations of Rowlatt, J., in *Brown's case* [1] :—

"There is no doubt that the general scheme of the income tax is that it is payable in respect of a source of income existing in the year of assessment, though the amount is often measured by the results of the previous years—"

were, under the English Act, appropriate. The Court next rejected the contention of the Crown that the Indian Income-tax Act, 1922 (which was applicable to the case), maintained the general scheme of the English Act of putting tax upon income derived during the year of assessment. It was pointed out that the tax under the Indian Act of 1922 was on the income of the previous year and it was not a standard by which the next year's income was to be computed. It was pointed out that this fundamental distinction made a complete change in the manner of assessment under the Indian Act of 1922. The Court relied on the rules under which adjustments were permissible under the Indian Act of 1918, but which were dropped in the Act of 1922. It was held that while Sections 6 to 12 stated the heads of income, which are chargeable, and which authorised specific allowances or exclusions, the tax was one on the total income of the assessee. The tax was not paid on each of the heads. It was pointed out that there may be difficulties in computing income and the allowances permitted may not work out equitably. With that aspect the Court cannot be concerned in construing the plain meaning of the sections of the Act. In dealing with the exemptions allowed under Sections 9 and 10 Rankin, C. J., observed as follows [2] :—

"It seems to me to be reasonably clear in Sections 9 and 10 that though the present tense is used throughout, the sections are to be applied to the state of facts in the 'previous year' or in the case of an exceptional assessment under Section 25 (1) a completed portion of the year of assessment. They afford no reasonable ground for a contention that the particular sources numbered (iii) and (iv) must persist

(1) [1919] 2 K.B. 497, at p. 509. (2) (1927) 54 Cal. 630, at p. 643.

throughout two years in order to be chargeable. It is here that it is important to remember that the income-tax is one tax as Section 3 shows it to be."

In numerous cases the Privy Council has repeatedly cautioned the Indian Courts not to rely on English cases which are based on technical rules and provisions of English law of taxation. The observations of Rowlatt, J., in *Bennett* v. *Ogston*[1] themselves show why the receipts should not be considered income if the profession or vocation had ceased in the assessment year. The learned Judge observed (page 378) :—

"... they are the receipts of the business while it lasted, they are arrears of that business...and are taken to be covered by the assessment made during the life of the business, whether that assessment was made on the basis of bookings or on the basis of receipts."

On the principle that in England the current year's income is assessed and taxed, while the business is going on during that year, the income is taken to be covered by the assessment and there can arise no question of taxing it again at any later date. This emphasises the distinct principle of taxation under the English Act. The observations in *Hillerns and Fowler* v. *Murray*[2] are also explicable on the same footing. On the other hand, Lord Wright in delivering the judgment of the Privy Council in *Kamakshya Narain Singh's case*[3] observed: "Income, again, may consist of a series of separate receipts, as it generally does in the case of professional earnings." He did not draw a distinction between receipts during the time the assessee was carrying on a profession and after he had ceased to practise.

In my opinion, the question whether a particular amount is income or not has nothing to do with the time of its receipt. The question of receipt is material only for the purpose of determining whether on that amount tax is to be levied under the Act in the year of assessment. The question of receipt may be material, not for the purpose of determining whether it is income or not, but for computing it in the assessment year. If the assessee, in respect of his business or income from other sources, keeps his accounts on the mercantile basis, his income is computed on the footing of accrual. If, on the other hand, he keeps his accounts on the footing of receipts, his income is computed in that manner. There is no difficulty in reading Sections 10, 12 and 13 together for the purpose of computation. The allowances permitted under Sections 10 and 12, if the method of accounting is the mercantile method, will have to be computed according to that method. If, however, the computation is on the method of receipts, all those

(1) (1930) 15 Tax Cas. 374.
(2) (1932) 17 Tax Cas. 77.
(3) (1943) 11 I.T.R. 513.

allowances must be allowed in the year of disbursements, irrespective of the question when the liability to pay the same arose. Any other construction will result in a hopeless confusion. If the method of accounting is receipts, on the credit side, irrespective of the question whether the source exists or not, the receipt, which is income, is credited. On the debit side disbursements or "deductions," permitted in Section 10 or 12, irrespective of the question when the liability to pay the same arose, have to be entered. The balance so arrived at has to be taxed. It need not be repeated that the gross receipts are not to be taxed. If the taxing authorities have accepted the method of accounting as cash receipts and cash payments, this is the only way in which the "total income" could be properly computed in the assessment year under the Indian Income-tax Act.

I do not think this construction of Section 4 results in making two incomes out of the same amount, as argued on behalf of the assessee. Clauses (a), (b) and (c) of sub-section (1) are connected by the word "or" and not "and." The result is that in the previous year's income, which is to be included in the "total income," the amount can be entered if it falls under (a), or (b) or (c). It must be recognised that if a particular amount is assessed and taxed under (a), or (b) or (c), the same amount cannot be taxed under a different heading either in the same year or in a different year. It is therefore futile to contend that the result of the construction suggested above makes the same income liable to tax under two heads. The contention that under the Indian Act the method of accrual only is accepted as the method of taxation is unsound, because Section 4 (1) (a) expressly makes the receipts of income, from whatever source derived, taxable if it is received in the "previous year." The words there used clearly mean the income received for the first time, if the method of accounting is not mercantile basis. On that amount the assessee will not be taxed on the accrual basis under Section 4 (1) (b), but the taxation will be under Section 4 (1) (a) only. As pointed out in *Behari Lal Mullick, In re*[1], the Income-tax Act of 1918 was framed to tax the income of the current year. To ascertain the amount the income of the previous year or the average of certain years was taken as a measure. The tax, however, was on the income of the current year. That scheme was changed by the Act of 1922 and thereafter in fact it was the income of the previous year which was taxed. On that ground alone the relief granted under Section 26 of the Act could be justified and reconciled. In 1939 the Act was again amended. One of the principal objects of the amendment of the various sections was

(1) (1927) 54 Cal. 680.

to tax the foreign income of a resident or the foreign income of a non-resident brought into British India. We are not directly concerned with the motives of the Legislature but we are bound by the effects of the amendments. The amendments made by that Act further emphasise the view that under the Indian Act 'accrual' is not the only basis for computation and taxation. There appears no justification for the contention that Section 4 (1) (a) is limited to receipts by non-residents only. If that was the intention of the Legislature, clause (a) should be after Section 4 (1) (c) and not where it is placed. The separate scheme of computation found in Sections 7 to 9 on the one hand, and Sections 10 to 12 read with Section 13 on the other hand, also negatives that contention. Again the fact that Section 4 (1) (b) is confined to "persons ordinarily resident" and Section 4 (1) (c) is confined to persons "not ordinarily resident" emphasises the construction that Section 4 (1) (a) is of general application and not limited to one of those two classes of persons only.

Neither side relied on Section 25 of the Act. This course appears to have been advisedly adopted because it is a permissive right given to the taxing authorities to prevent a man escaping assessment, if he proposes to close his business and leave British India in the middle of a year. In my opinion that section, however, does not preclude the authorities from proceeding with the assessment of an assessee, against whom the machinery of that section is not used, under the other sections of the Act.

In my opinion, therefore, the conclusion of the Commissioner is right and the answer to the question must be in the affirmative, with this reservation that the gross outstanding fees are not taxable but they are subject to the deductions permitted under Section 10, in view of the fact that the method of accounting regularly employed by the assessee was the cash receipts basis.

CHAGLA, J.—The question for our determination in this reference is whether the receipts from a business or profession which has been discontinued are income liable to tax under the Indian Income-tax Act. It has been contended by the assessee that the profits or gains of a business or profession are only taxable provided the business or profession was carried on at the time the profits or gains were received. It has been further contended that the whole scheme of the Income-tax Act is to tax income only so long as the source from which the income was derived is in existence. If the income is received from a defunct source, then that income is not liable to tax.

In order to understand and appreciate this contention of the assessee, it is necessary to consider the scheme of the taxing statute.

Section 3 of the Act provides that the tax shall be charged at the rate mentioned in the Finance Act. Section 4, which defines the applicability of the Act, lays down the conditions of chargeability. It states what the total income of the assessee in any previous year is. That section deals in the first instance with any person whether he be a resident or non-resident in British India. Then it deals with a resident in British India and finally with a person not resident in British India. In the case of any person the conditions of chargeability shall be that the income shall be received or deemed to be received in British India in the previous year. Having dealt with the receipt of income in British India and made it liable to tax in the case of every person, the section then proceeds to deal with accrual of income and in clause (b) it deals with accrual in the case of a resident in British India and in clause (c) in the case of a non-resident in British India. Then under sub-section (3) it provides various exceptions which need not be included in the total income of the assessee. Therefore, in the first instance, it is necessary to ascertain whether what is sought to be charged as income under Section 4 satisfies the conditions of chargeability laid down in that section.

"Income" is nowhere defined in the Act. Even the plain natural meaning of "income" is so full of connotations that it is not always easy to say with precision what exactly "income" means. Even so high a tribunal as the Privy Council when it has launched upon the adventurous task of defining "income" has found itself confronted with serious difficulties.

In *Commissioner of Income-tax* v. *Shaw Wallace & Co.*[1], Sir George Lowndes delivering the judgment of the Privy Council defined "income" as a periodical monetary return "coming in" with some sort of regularity, or expected regularity, from definite sources. He likened "income" pictorially to the fruit of a tree, or the crop of a field. He further points out that the expansion of "income" into income, profits and gains is more a matter of words than of substance. In *Gopal Saran* v. *Commissioner of Income-tax*[2], the Privy Council went as far as saying that anything which can properly be described as income is taxable under the Act unless expressly exempted. Lord Wright in the judgment of the Privy Council in *Kamakshya Narain Singh* v. *Commissioner of Income-tax, Bihar and Orissa*[3], appreciates the difficulty of defining "income" and concedes that it is perhaps impossible to define it in any precise general formula, but he says that it is a word of the broadest connotation. He rather disapproves of Sir George Lowndes' pictorial language and sounds a note of warning against using picturesque similes to limit the true character of income in general. He

(1) (1932) 59 I.A. 206. (2) (1935) 3 I.T.R. 237. (3) (1943) 11 I.T.R. 513.

gives several instances of what "income" might be, and it is rather pertinent to note that he considers a series of separate receipts in the case of professional earnings as income.

The first question then is: are the outstanding professional fees which were realized by the assessee during the year under assessment income within the meaning of Section 4 of the Act? It has not been disputed and it cannot be disputed that these professional fees would have undoubtedly been "income" if the assessee had been carrying on his profession as a consulting civil engineer in the accounting year. It is also admitted that when these fees accrued to the assessee they were income, but he was not taxed with regard to these fees because he was maintaining his accounts on a cash basis and not on a mercantile basis, which right is given to him under Section 13 of the Act. It is difficult to see how or why these receipts which would be "income" if the business was going on should cease to be "income" merely because that business had ceased at the time these receipts were collected. Section 4 refers to all income, profits and gains from whatever source derived. This particular income was derived from the profession of the assessee. Section 4 does not lay down as a condition of chargeability that the source should be in existence at the time the income is received. The only two conditions which are imposed by that section are that the receipt must be income and it must be received in British India during the previous year. In this case it is not disputed that the assessee received the amount in question in British India during the previous year and it was an amount derived from a particular source, namely, his profession, although that source had ceased to exist at the time when the amount was received.

A rather ingenious construction of Section 4 was suggested by Sir Jamshedji Kanga on behalf of the assessee. He argued that sub-clause (a) of Section 4 only applied to persons not resident in British India and that in the case of persons resident in British India the only income chargeable was that which accrued or arose or was deemed to accrue or arise in British India during the previous year. It was therefore suggested that in India as in England all assessment of residents in this country was on the accrual basis and the cash basis permitted under Section 13 was merely a method of arriving at the income. It was therefore contended that the assessee could only be assessed with regard to income which accrued to him, and as his business had come to an end, there could be no accrual of income from that source. Such a construction, in my opinion, is patently opposed to the scheme of Section 4 and to the other provisions of the Act. If receipt of income was intended to apply only to non-residents, then it is difficult to

understand the use of the language "any person" and also why this particular provision was not inserted in sub-clause (c) which deals with the case of non-residents. Further as Section 13 permits of the cash method of accounting in the case of business and other sources provided in Sections 10 and 12, the Legislature had to make both actual receipts in certain cases and accrual of income in other cases liable to tax which it has done under Section 4.

Whereas Section 4 lays down the conditions of chargeability, Section 6 deals with the manner of chargeability; and to use the language of their Lordships of the Privy Council in *Commissioner of Income-tax, Bombay Presidency and Aden* v. *Chunilal B. Mehta* [1],

"The effect of Section 6 is to classify profits and gains under different heads for the purpose of providing for each appropriate rules for computing the amount."

Therefore once it is ascertained that the amount is income under Section 4, the next step is to classify it under one of the heads mentioned in Section 6. This classification is solely for the purpose of computing the amount of income. Sections 6 to 12 provide a machinery for computation for every species of income which is made chargeable under Section 4. In the first instance, there are four specific heads under Section 6; and even if a particular kind of income does not fall under any of these four specific heads, it would fall under the wide residual head provided under Section 12. As pointed out by Lord Russell of Killowen delivering the judgment of the Privy Council in *Probhat Chandra Barua* v. *The King-Emperor* [2], Section 12 describes

"a true residuary group embracing within it all sources of income, profits and gains provided the Act applies to them, *i.e.*, provided that they accrue or arise or are received in British India or are deemed to accrue or arise or to be received in British India, as provided by Section 4, sub-section (1), and are not exempted by virtue of Section 4, sub-section (3)."

It would not be true to say that Sections 6 to 12 in any way control or limit the conditions of chargeability laid down in Section 4 of the Act. In the first place, as I have already pointed out, these sections merely provide various heads under which different income is to be classified for the purpose of computation, and the definition of a head cannot possibly control the meaning of income as referred to in Section 4 of the Act. Further the very presence of a true residuary head under Section 12 makes it impossible for any income which falls under

(1) (1938) 65 I.A. 332, at p. 347; 6 I.T.R. 521, at p. 529.
(2) (1930) 57 I.A. 228, at p. 239.

Section 4 to escape from falling under one of the heads under Section 6.

Unfortunately the language used by the Privy Council in *Probhat Chandra Barua* v. *The King-Emperor*[1] has afforded some basis to Sir Jamshedji Kanga to raise an argument that Section 6 is the real charging section and that it is only that income which satisfies the conditions laid down in Sections 6 to 12 which is liable to tax under the Act. In that case their Lordships said that although Chapter I of the Act was entitled "Charge of Income-tax," the real charging section was Section 6 which occurred in Chapter III. As I have already pointed out, in a later Privy Council case, *Commissioner of Income-tax, Bombay* v. *Chunilal B. Mehta*[2], their Lordships have taken quite a different view of the true effect of Section 6. But it must also be remembered that when these observations were made by the Privy Council it was dealing with the Act as unamended by the Act of 1939, and under the old Act the language of Section 4 was different. Section 4, as it then stood, provided that "this Act shall apply to all income, profits or gains, as described or comprised in Section 6, from whatever source derived, accruing or arising, or received in British India, or deemed under the provisions of this Act to accrue, or arise, or to be received in British India."

Under the present section reference to Section 6 has been removed, and we have the phrase "Subject to the provisions of this Act." It is true that even under the present section "Subject to the provisions of this Act" would necessarily include the provisions of Section 6. But as under the old Act the income referred to in Section 4 was specifically confined to that described or comprised in Section 6, it is quite understandable why Lord Russell should refer to Section 6 as the true charging section as it was given that high place of honour in Section 4. Not only was Section 4 amended by the Act of 1939 but also Section 12. Under the old Act the other sources were in respect of income, profits and gains of every kind and from every source to which the Act applied. Under the amended Act income, profits and gains of every kind which may be included in the total income and are not included under any of the specific heads mentioned in Section 6 may be included under this head. While it is true that the amendments I have just referred to do not in any way extend the definition or the import of income under the Act, whatever the position might have been under the old Act, it is perfectly clear that under the Act with which we are concerned Section 6 is not a charging

(1) (1930) 57 I.A. 228, p. 239.

(2) (1938) 65 I.A. 332, at p. 347; 6 I.T.R. 521, at p. 529.

section and it does not in any way affect or control the conditions of chargeability.

The next question is: do these receipts fall under the head "Profits and gains of business, profession or vocation?" This head only applies to a business, profession or vocation carried on by the assessee. In the case before us the profession was undoubtedly carried on by the assessee. The material question is whether the section requires that it should be carried on at or up to a particular point of time. Three possible constructions have been suggested at the bar: *first*, that the expression "carried on by him" merely connects the assessee with the business or, in other words, it is merely a paraphrase of "his business, profession or vocation"; *second*, that it must be carried on at any time during the year of assessment; and, *third*, that it must be carried on at the time the profits or gains of the business or profession were received. It is rather difficult to accept the first construction because an assessee cannot carry on the business of anyone else except his own, and if the only object of the Legislature was to refer to his business, the language used seems to be particularly inapt. But I see no reason to read in the expression "carried on by him" the words "at the time the income, profits and gains are received." All that is required is that it must be a business which is carried on by the assessee in the previous year—the year under assessment. In this case the business was carried on by the assessee in the previous year up to February 15, 1938. It is true that subsequent to February 15, 1938, for the rest of the accounting period up to December 31, 1938, the assessee did not carry on the business. But the section does not require, as I read it, that it must be carried on throughout the year under assessment. This particular source was in existence in the accounting year, and the assessee is liable to pay tax on all income, profits or gains derived from all sources in existence in the year under assessment.

Even if this income does not fall under the head of business, profession or vocation, if it is income at all, it must necessarily fall under the residuary head under Section 12. This head, as I have already pointed out, refers to income, profits and gains of every kind and the only condition required is that it cannot be included under any of the preceding heads referred to in Sections 7 to 10.

It is possible to dispose of this reference on the short point that as the profession was carried on by the assessee in the year under assessment, the profits and gains of that profession are liable to tax. As the matter was debated at great length and as we have had the advantage of listening to very learned arguments from counsel on both sides, I should like to add that in my opinion, even if the business or

the profession had been discontinued prior to the accounting year, I see no reason why the profits and gains of such discontinued business or profession should not fall under the residuary head under Section 12, if in fact they were received during the year under assessment.

It has been contended that what the assessee received was gross receipts and these do not constitute profits and gains of a business or profession. It has got to be remembered that as this assessee had adopted the cash basis as his method of accounting, he would be taxed on the actual receipts and not on any accrual basis. It is true that he would not be liable to pay the tax on gross receipts, but he would be permitted to deduct therefrom all permissible allowances under Section 10 of the Act. In the case before us the assessee received the sum of Rs. 12,302 from his profession. There is no reason why he should not deduct from this sum any permissible expenditure incurred by him for the purpose of his profession. If in fact he incurred no expenditure for the purpose of his profession in the year under assessment, then the receipts constitute the profits and gains of his profession.

The contentions of the assessee have received considerable support from the observations of Mr. Justice Rowlatt reported in two English cases, *Bennett* v. *Ogston* [1] and *Hillerns and Fowler* v. *Murray* [2], and from the fact that in England the outstandings remaining to be collected by a professional man, after he has ceased to practise that profession, are not assessable to income-tax. The Privy Council has often sounded a note of warning against relying on English cases based on English income-tax statutes for the purpose of construing our own statute. As stated by their Lordships in *Commissioner of Income-tax* v. *Shaw Wallace & Co.*[3], the Indian Act is not in *pari materia*. English decisions are only helpful when they enunciate a principle which is wide enough to be applicable both here and in England notwithstanding the fact that the taxing statutes of the two countries are entirely different and are based upon technical rules which have very little in common.

The reason why outstanding fees of a profession collected after its discontinuance are not taxed in England is that they are taken to be covered by the assessment made during the life of the profession as pointed out by Mr. Justice Rowlatt in *Bennett* v. *Ogston* [1]. And in *Hillerns and Fowler* v. *Murray* [2], Lord Justice Greer at page 89 concedes that these outstandings are income and that in England some people by a stroke of good fortune are enabled to escape paying tax upon income that they have made by reason of a technical application of the provisions of the taxing Acts.

(1) (1930) 15 Tax Cas. 374. (2) (1932) 17 Tax Cas. 77. (3) (1932) 59 I.A. 206.

The fundamental difference between our taxing statute and the English statute must always be borne in mind. Our Act taxes the income of the previous year, the English Act taxes the income of the current year; and as the actual income of the current year must to a large extent be estimated by reference to various considerations and not to the actual income earned in that year, income in England has to be computed on an accrual and not on a receipt basis. In the well-known case of *Behari Lal Mullick, In re*[1], Sir George Rankin, Chief Justice, explains why in England the source of the income has to be in existence in the year of assessment. At page 636 he says:—

"If in the year of assessment the assessee had derived some income from a particular source the amount for purposes of taxation might have to be computed at least provisionally by reference to his income from that source in one or more of the years immediately preceding. If, however, the assessee in the year of assessment derived no income from a source which in the previous years had yielded income the statutory rules as to computation of the present and future by reference to the past did not apply so as to impute to the year of assessment an income which did not exist at all. The basis and subject-matter of the tax was the income in the year of assessment. As a matter of law this is true because it is the true construction of the English statutes and for no other reason."

It has been strenuously urged by Sir Jamshedji Kanga that the Privy Council in *Commissioner of Income-tax* v. *Shaw Wallace & Co.*[2], has decided that when a business comes to an end any income derived from such a business is not liable to tax. The facts of that case clearly show that the two sums received by the assessee company were received not out of any business carried on by them but as a solatium for the compulsory cessation of its business. As they did not arise from any business or from any continuous exercise of an activity, the Privy Council came to the conclusion that the sums did not represent income, profits or gains within the meaning of the Act and liable to tax. It is not permissible in my opinion to extend the effect of this decision to mean that even if these two sums had been received as a result of the carrying on of the assessees' business still they would not have been liable to tax merely because that business had ceased at the time when these two sums were received.

Strong reliance was placed by Sir Jamshedji Kanga on a judgment of Mr. Justice Din Mohammad of the Punjab High Court in *B. C. G. A. (Punjab) Ltd.* v. *Commissioner of Income-tax, Punjab*[3]. In that case the assessee closed his business in 1931 as he suffered heavy losses. He accepted bonds in respect of moneys outstanding from

(1) (1927) 54 Cal. 630. (2) (1932) 59 I.A. 206. (3) (1937) 5 I.T.R. 279.

some of the debtors. These bonds became time-barred in the accounting year, and the assessee claimed to set off those losses against the profits of another business which he was still carrying on. Mr. Justice Din Mohammad held that the assessee could not do so as he could not set off the losses of a discontinued business against the profits and gains of a current business inasmuch as Section 10 of the Income-tax Act dealt with businesses that were being carried on and not with businesses which had ceased to exist. Mr. Justice Din Mohammad was dealing with a case of a set-off and not the question of income of a discontinued business. But in any case all that Mr. Justice Din Mohammad decided was that Section 10 requires that the business should not have ceased to exist in the year under assessment and should be carried on by the assessee. In the case before us, as I have pointed out, the profession of the assessee had not ceased to exist and was being carried on at least for a part of the year under assessment.

I, therefore, agree with my learned brother Kania that the question raised in this reference should be answered as he has suggested. I have had the advantage of reading the judgment just delivered by the learned Chief Justice. I have given it my most careful attention. It is with the very greatest reluctance that I find myself in disagreement with the conclusion reached by him.

Reference answered accordingly.

[In the Madras High Court.]

K. AR. S. T. ARUNACHALAM CHETTIAR

v.

COMMISSIONER OF INCOME-TAX, MADRAS.

Sir Lionel Leach, C. J., and Patanjali Sastri, J.

November 9, 1945.

Money-lending Business—Sale of Property Forming Part of Capital of Money-lending Business—Profit, whether Liable to Income-tax.

The assessee, who was a member of a Hindu undivided family carrying on a money-lending business, started, after partition, a separate money-lending business of his own in Burma. Subsequently he received from his father as gift a rubber and a cocoanut plantation in Malaya in addition to a share in the assets of the money-lending business in Malaya which his father had received as his share at the time of partition. The assessee thereupon started a money-lending business in Malaya and entered in the books of account of his money-lending business the values of the two plantations and treated them as part

of the capital of the business. In these accounts the expenses of running the estate were debited and the profits accruing therefrom were entered as profits of the business. In the year of account the assessee sold a portion of the rubber plantation and entered the sale proceeds in the accounts of his business. The question was whether the profit arising on the sale of a part of the rubber plantation was liable to income-tax:

Held, *that the profit was liable to income-tax inasmuch as the plantations formed part of the capital of the assessee's money-lending business and the profit was included in the profits of the business.*

Case referred to the High Court by the Income-tax Appellate Tribunal, Madras Bench, under Section 66 (1) of the Indian Income-tax Act, 1922 (Act XI of 1922), as amended by Section 92 of the Income-tax (Amendment) Act, 1939 (Act VII of 1939), in Application 66 R. A. No. 39 (Madras) of 1943-44 on its file relating to year of assessment 1941-42, for decision on the following question of law, namely:—

" Whether in the circumstances of this case, the profit arising on sale of the property was liable to income-tax. "

STATEMENT OF CASE.

" This is an application under Section 66 for reference of the following questions of law propounded by the applicant:—

' Whether the conclusion of the Appellate Tribunal that the rubber gardens obtained by way of gift from the assessee's father was circulating capital is correct in law and whether profit on sale of such property is income liable to tax; and whether the mere entry in the money-lending business of an item of immovable property got by gift from father was a material on which the conclusion that sale of the property was a revenue sale could be based.'

2. The respondent states that the only question of law which arises is the following :—

' Whether in the circumstances of this case, the profit arising on sale of the property was liable to income-tax.'

3. The facts of this case are that the applicant originally was a member of a Hindu undivided family which consisted of himself, his father Chidambaram Chettiar, and his brother Narayanan Chettiar. In 1925, the family was disrupted. Before disruption this family was carrying on money-lending business in partnership with an outsider at Battu Pahat, in Malaya. At the time of disruption the entire assets of the family money-lending business were distributed between the members. The interest in the partnership business at Battu Pahat fell exclusively to the father's share. After disruption, the father and the sons started their independent business of money-lending.

4. In 1939, Chidambaram Chettiar, the father, decided to retire from business. He decided to divide the business assets, and other property between his two sons, retaining some amount of cash for himself. In pursuance of his decision, he gifted some properties which formed part of his money-lending assets to the applicant and some other properties to his brother Narayanan. On receipt of these gifts, the brothers, who had hitherto kept away from Battu Pahat, decided to start their independent businesses at that place. After they had set up the new businesses, the applicant decided to sell some of the properties received by him as a gift from his father and these properties were actually sold in the accounting year.

5. For the purpose of 1941-42 assessment, the Income-tax Officer treated the properties in question as a part of the stock-in-trade of the applicant and the profit on the sale thereof was included by him in the assessable income. On these facts the Bench came to the conclusion that the profits earned by the sale of these properties should be treated as a receipt in the nature of revenue receipt.

6. We agree with the respondent that the proper question that should be framed and referred to the Honourable High Court, is the following :—

'Whether in the circumstances of this case, the profit arising on sale of the property was liable to income-tax.' "

This reference came up for hearing on the 2nd day of March 1945, and the Court made the following :

ORDER.

(Order of the Court was delivered by the Honourable the Chief Justice).

For the purpose of deciding the question referred in this case we think it necessary to know whether the expenses of the rubber plantations were debited to the assessee's money-lending business and whether the income from the plantations was brought in as part of the profits of that business. In these circumstances we refer the case back to the Income-tax Appellate Tribunal under the provisions of Section 66 (4) for a statement of the facts.

The reference will stand adjourned until this further statement has been received.

In compliance with the above order the Income-tax Appellate Tribunal submitted the following further statement of facts :—

FURTHER STATEMENT OF CASE.

"This reference went up for hearing before the Honourable Judges of the High Court of Judicature at Madras on 2nd March 1945, but the Honourable the High Court has referred this case back to the Tribunal, under the provisions of Section 66 (4), for a statement of further

facts. The points on which the Honourable High Court requires information are whether the expenses of the rubber plantations were debited to the assessee's money-lending business and whether the income from the plantations was brought in as part of the profits of that business.

2. The parties to this application were given a further opportunity of being heard, and in response to the notices served upon them, they were present for hearing before us today.

3. The books of account of the applicant were produced and from this it was found that the income from the rubber gardens (after deducting the expenses thereout) was taken over to the general profit and loss account. The advocate for the applicant contended that the books of account did not relate to his money-lending business and that he had no money-lending business until the gardens were sold and the proceeds of the same were made available for the purpose of starting such money-lending business. He further stated that the income arising from interest, etc., which was credited in the profit and loss account appearing in the books produced before us and interest or income arising from the outstandings were gifted to the applicant by his father. The applicant did not consider these to be his money-lending assets. The special counsel for the department has taken objection to the applicant's contention and states that the applicant is attempting to raise a new issue by questioning the existence of a money-lending business. According to him, that was never a question raised by the applicant at any earlier stage or even before the Honourable High Court and the applicant was not entitled to raise that issue at this stage. We also consider that the question raised by the advocate regarding the existence of the money-lending business prior to the sale of the rubber gardens is improper, particularly in view of the use of the words "money-lending business" by the applicant himself in the question referred to by him in his reference application. We will repeat his question hereunder:—

'Whether the conclusion of the Appellate Tribunal that the rubber gardens obtained by way of gift from the assessee's father was circulating capital is correct in law and whether profit on sale of such property is income liable to tax; and whether the mere entry in the money-lending business of an item of immovable property got by gift from father was a material on which the conclusion that sale of the property was a revenue sale could be based.'

4. Both the parties have come to an agreement with regard to the points raised by the Honourable High Court in their order referring the case back to us and it is admitted that the income as well as the expenditure of the rubber plantations appear in the one set of books of account produced before us which are for both the

money-lending as well as the plantation business. The enquiry of the Honourable High Court is, therefore, answered by stating that the expenses of the rubber plantations were debited in the assessee's money-lending business and the income from the plantations was brought in as part of the profits of that business.

This case came up for final hearing after the submission of the further statement of facts by the Income-tax Appellate Tribunal and the Court delivered the following judgment.

M. Subbaraya Aiyar, for the assessee.

C. S. Rama Rao Sahib, for the Commissioner.

JUDGMENT.

(Judgment of the Court was delivered by the Honourable the Chief Justice).

The Income-tax Appellate Tribunal has submitted the further statement of facts called for by this Court in its order of the 2nd March 1945. The facts are now clear and they may be stated shortly as follows :—

The assessee, his father and his brother Narayanan Chettiar constituted an undivided Hindu family, but partition was effected in 1925. Before the separation the family had carried on a money-lending business in partnership with another person at Battu Pahat in Malaya. Under the terms of the separation the entire assets of the money-lending business at Battu Pahat fell to the father's share. The sons then started separate money-lending businesses of their own in Burma. In 1939 the father decided to retire from business. In addition to the assets of the money-lending business at Battu Pahat, he was possessed of certain rubber and cocoanut plantations. After reserving for himself sufficient to live upon, he divided the rest of his assets between his two sons. Each of them received a rubber plantation and a cocoanut plantation at Battu Pahat in addition to equal shares in the assets of the money-lending business. Thereupon each of them started a money-lending business at Battu Pahat. The assessee entered in the books of account of his money-lending business the values of the two plantations which had been given to him. They were treated as being part of the capital of the money-lending business. In these accounts the expenses of running the estate were debited and the profits accruing therefrom were entered as profits of the money-lending business. In the year of account the assessee sold a portion of the rubber plantation and entered the sale proceeds in the accounts of his business. The sale showed a profit. The question in this case is whether this profit was liable to income-tax. The Tribunal held that it was, but referred to this Court for decision the following question :—

"Whether in the circumstances of this case, the profit arising on sale of the property was liable to income-tax."

We consider that the decision of the Tribunal was clearly right. The plantations formed part of the assessee's capital of his money-lending business and the profit made on the sale of a part of the rubber plantation was included in the profits of the business. We answer the question referred in the affirmative.

The assessee must pay the costs of the Commissioner, Rs. 250.

Reference answered in the affirmative.

[IN THE LAHORE HIGH COURT.]

R. S. MUNSHI GULAB SINGH AND SONS

v.

COMMISSIONER OF INCOME-TAX, LAHORE.

DIN MOHAMMAD and MEHR CHAND MAHAJAN, JJ.

October 9, 1945.

INDIAN INCOME-TAX ACT (XI OF 1922), SECS. 14, 10 (2) (ix) (BEFORE AMENDMENT IN 1939); SEC. 10 (2) (xii) (AFTER AMENDMENT IN 1939)—BUSINESS EXPENDITURE—PAYMENT TO AVOID COMPETITION—PRINTING AND PUBLISHING CONCERN—PAYMENT TO COMPETITORS FOR QUOTING UNIFORM RATES IN TENDERS—SUBSCRIPTIONS PAID TO SCHOOLS FOR PRESCRIBING PUBLISHED TEXT BOOKS—WHETHER ALLOWABLE—EXEMPTION—SUMS RECEIVED AS MEMBER OF HINDU UNDIVIDED FAMILY—MAINTENANCE ALLOWANCE PAID TO WIDOWED MOTHER AND STEP-MOTHER UNDER AWARD CHARGED ON PROPERTY.

The assessee, a Hindu undivided family consisting of a father and his sons, was the owner of an ancestral printing and publishing concern. In order to secure full time work for its press and in the interest of its business, the assessee entered into an arrangement with two other rival printing and publishing concerns by which the parties agreed to quote uniform rates in the tenders given to Government for printing and publishing work and the assessee agreed to pay its competitors, irrespective of whether there was actual loss or profit, a certain share in the estimated profit which was arrived at by deducting certain agreed cost contemplated to be incurred in the execution of the job from the amount of the tendered cost. The Appellate Tribunal found that the payments were made by the assessee to shut out competition with a view to secure work which would enable it to earn profits or to earn more profits than could otherwise be earned.

Held, *that the payments made to the competitors were expenditure not of a capital nature laid out wholly and exclusively for the purpose of the business and as such allowable under Section 10 (2) (xii) of the Income-tax Act after its amendment in 1939 and under Section 10 (2) (ix) of the Act before its amendment in 1939. Expenditure incurred in obtaining each new printing contract was not in the nature of capital expenditure incurred for acquiring a business, nor was the payment made to the competitors a payment out of profits or a sharing of profits.*

Guest, Keen and Nettlefolds v. *Fowler* [1910] (5 Tax Cas. 511) relied on.

The assessee further paid certain amounts by way of subscriptions to certain schools which agreed to prescribe for their classes school books published by it. The amount payable to each school was calculated after taking into consideration the number of boys in each class for which the assessee's books would be prescribed :

Held, *that the subscriptions paid to the schools were expenditure (not being in the nature of capital expenditure) laid out wholly and exclusively for the purpose of the business and as such allowable under Section 10 (2) (xii) of the Act after its amendment in 1939 as well as under Section 10 (2) (ix) of the Act before its amendment in 1939.*

A partition award, by which the karta *of the assessee family partitioned the family estate with his brothers, directed the brothers to pay a certain amount monthly as maintenance to their widowed mother and step-mother and made the amount of maintenance a charge on some property* :

Held, *following* HIRA LAL, *In re* [1945] (13 I.T.R. 512), *that the payments made by the* karta *under the award in discharge of his share of liability should not be taxed as his income but must be excluded from his assessable income.*

Cases referred to :—

Alaganan Chetty *v.* Commissioner of Income-tax, Madras [1928] (3 I.T.C. 44 ; 55 M.L.J. 66 ; 27 L.W. 776 ; A.I.R. 1928 Mad. 902).

Atherton *v.* British Insulated and Helsby Cables Ltd. [1925] (10 Tax Cas. 155 ; [1925] 1 K.B. 421 ; 94 L.J.K.B. 319 ; 132 L.T. 288 ; [1926] A.C. 205).

City of London Contract Corporation *v.* Styles [1887] (2 Tax Cas. 239 ; 4 T.L.R. 51).

Collins *v.* Joseph Adamson and Company ([1938] 1 K.B. 477 ; 7 I.T.R. 92).

Gopinath Vir Bhan *v.* Commissioner of Income-tax, Punjab [1938] (6 I.T.R. 243 ; I.L.R. [1938] Lah. 426 ; 40 P.L.R. 228 ; A.I.R. 1938 Lah. 530).

Granite Supply Association *v.* Kitton [1905] (5 Tax Cas. 168 ; 43 Sc.L.R. 65).

Gresham Life Assurance Society *v.* Styles [1892] (3 Tax Cas. 185 ; [1892] A.C. 309 ; 62 L.J.Q.B. 41 ; 67 L.T. 479 ; 41 W.R. 270).

Guest, Keen and Nettlefolds *v.* Fowler ([1910] 1 K.B. 713 ; 5 Tax Cas. 511 ; 79 L.J.K.B. 563 ; 102 L.T. 361 ; 26 T.L.R. 337).

Hancock *v.* General Reversionary and Investment Company ([1919] 1 K.B. 25 ; 88 L.J.K.B. 248 ; 119 L.T. 737 ; 35 T.L.R. 11 ; 7 Tax Cas. 358).

Hira Lal, *In re* [1945] (13 I.T.R. 512).

Moore and Company *v.* Hare [1914] (6 Tax Cas. 572 ; (1915) Sess. Cas. 91 ; 52 Sc.L.R. 59).

Ounsworth *v.* Vickers ([1915] 3 K.B. 267; 84 L.J.K.B. 2036; 113 L.T. 865; 6 Tax Cas. 671).

Pondicherry Railway Co., Ltd. *v.* Commissioner of Income-tax, Madras [1931] (I.L.R. 54 Mad. 691; 5 I.T.C. 363; 58 I.A. 239; 35 C.W.N. 895; 132 I.C. 619; A.I.R. 1931 P.C. 165).

Rowntree and Co., Ltd. *v.* Curtis ([1925] 1 K.B. 328; 93 L.J.K.B. 57; 129 L.T. 530; 131 L.T. 41; 40 T.L.R. 363; [1924] W.N. 89; 8 Tax Cas. 678).

Smith *v.* Incorporated Council of Law Reporting ([1914] 3 K.B. 674; 83 L.J.K.B. 1721; 111 L.T. 848; 30 T.L.R. 588; 6 Tax Cas. 477).

Southwell *v.* Savill Brothers ([1901] 2 K.B. 349; 70 L.J.K B. 815; 85 L.T. 167; 49 W.R. 682; 4 Tax Cas. 430).

Stott *v.* Hoddinott [1916] (7 Tax Cas. 85).

Tata Hydro Electric Agencies Ltd., Bombay *v.* Commissioner of Income-tax, Bombay [1937] (I.L.R. 1937 Bom. 388; 5 I.T.R. 202; 64 I. A. 215; 41 C.W.N. 774; 39 Bom. L.R. 775; 46 L.W. 60; 168 I.C. 173; A.I.R. 1937 P.C. 139; 1937, 2 M.L.J. 763).

Usher's Wiltshire Brewery Ltd. *v.* Bruce ([1914] 1 K.B. 357; [1914] 2 K.B. 891; 6 Tax Cas. 399; [1915] A.C. 433; 84 L.J.K.B. 417; 112 L.T. 651; 31 T.L.R. 104).

Vallambrosa Rubber Company *v.* Farmer [1910] (5 Tax Cas. 529; (1910) Sess. Cas. 519).

Case referred by the Income-tax Appellate Tribunal under Section 66 (1) of the Indian Income-tax Act (XI of 1922), as amended by Section 92 of the Income-tax (Amendment) Act, 1939 (VII of 1939): Civil Reference Case No. 2 of 1945.

STATEMENT OF CASE.

" These are four applications under Section 66 (1) of the Income-tax Act for reference to the High Court of Judicature at Lahore. The questions formulated are said to arise out of our orders under Section 33 of the Income-tax Act in R. A. A. No. 17 (Punjab) of 1943-44, R. A. A. No. 18 (Punjab) of 1943-44, R. A. A. No. 19 (Punjab) of 1943-44 and R. A. A. No. 20 (Punjab) of 1943-44, relating to the assessments of the applicant for the years 1938-39, 1939-40, 1940-41 and 1941-42 respectively. The same five questions have been framed in each of the applications for reference, inasmuch as the facts leading up to the questions are the same in the assessments for all the four years mentioned above. It will, therefore, be convenient to draft one statement of case instead of four. The decisions of their Lordships on the questions referred will govern the assessments for the four years.

2. The facts relevant to the questions formulated by the applicant may be stated in brief. The applicant Hindu undivided family carried on the business of printers and publishers; so do Messrs. Feroze Din & Sons and Messrs. Attar Chand Kapoor & Sons. Some payments were made by the applicant to Messrs. Feroze Din & Sons and Messrs. Attar Chand Kapoor & Sons. The exact nature of the payments was not clear from what the Income-tax authorities stated in their orders. The learned advocate, who appeared before us at the appeal stage, however, explained it to us. We were told that the establishment and some other expenses of the applicant were appreciably more than those of the two other

concerns, so that these two concerns could charge comparatively low rates for printing work and yet make profits, which was not possible for the applicant to do. If the two concerns quoted lower rates, some work would naturally go to them, which otherwise might have come to the applicant. If, on the other hand, equal rates were quoted by the applicant and the other two concerns, the applicant having a bigger and better known establishment would naturally get all the work that it could cope with, some of which would otherwise have gone to the other two concerns. In order, therefore, to secure full time work, and in the interest of its own business, the applicant induced the other two concerns to quote the same rates as the applicant by offering to pay to each of them something by way of compensation for loss of work, which would inevitably arise to them, as explained above. It was further explained that besides having such an undertaking regarding printing business with each of the other two concerns, the applicant had with Messrs. Attar Chand Kapoor a similar understanding regarding publication or "Book Depôt" business.

3. The exact basis of the computation of the amounts paid to the two concerns does not appear to be at all clear, and no explanation in this behalf was offered to us. There is nothing in writing between the applicant and the other two concerns to explain the understanding amongst them—only at the assessment for 1940-41, some sort of an agreement in regard to a particular printing contract was shown to the Income-tax Officer. The agreement was signed by three persons on behalf of the three concerns. It was an agreement "to undertake the printing of ballot papers of Gurdwara election, tender of which is to be submitted to the Government Press on the following terms......" It said that "a uniform rate as noted below shall be tendered." After mentioning the different tender rates for papers of different sizes, the agreement mentioned the different rates of costs, at which expenses were to be deducted from the gross receipts to find out net profits. Thus it was not the actual cost, but estimated cost at fixed rates, that was to be taken into account to find net profits, which were to be divided equally in three parts, each party getting a part. The Income-tax Officer held that "the alleged fact of partnership has not been indicated in the return filed, which completely roots out the claim in so far as the genuineness of the partnership is concerned." He further observed that "it is surprising that no amount has been paid to Messrs. Attar Chand Kapoor & Sons, nor has his account been credited with his share of income." There was nothing to show whether the applicant got the entire work, so that he alone had to pay to the other two parties. It was not explained why one of the partners got nothing.

It is also not known if that party got a portion of the work; if so, according to the agreement, the applicant should also have got his share of income from that party; but apparently he got nothing. Our conclusion was that the agreement was not acted upon in full, whatever its genesis might have been. In the circumstances, we held that the existence of this agreement during the accounting year for the 1940-41 assessment really made no difference.

4. The case for partnership was not seriously pressed before us at the appeal stage. In any event in the case of partnerships the amounts paid to partners cannot be claimed as revenue expenditure under the law.

5. Having regard to the nature of the payments, we held that the expenditure in question could not be said to have been incurred solely for the purposes of earning the profits and gains of the business [Section 10 (2) (ix) of the Income-tax Act before its amendment in 1939, which was the relevant section, under which the claim was made, so far as the 1938-39 assessment was concerned], or laid out or expended wholly and exclusively for the purpose of the business [Section 10 (2) (xii) of the Income-tax Act after its amendment in 1939, under which the claim was made, so far as the assessments for 1939-40, 1940-41, and 1941-42 were concerned]. We held that that expenditure was clearly incurred for *securing business* as distinct from earning profits from the business or carrying on the business. Our conclusion, therefore, was that the expenditure was not an admissible deduction under the Income-tax Act. We found support for our conclusion in the Full Bench decision of the Madras High Court in the case reported as *Rao Saheb Alaganan Chetty* v. *Commissioner of Income-tax, Madras*[1].

6. The applicant paid subscriptions to certain schools and claimed these payments as legitimate business deductions on the ground that the payments had been made in the "interest of business." Certain subscriptions were paid to certain schools, which agreed to prescribe for their classes school books published by the applicant. The amount of subscription to each school was said to be calculated having regard to the number of boys in each class for which the applicant's books would be prescribed. We were told that these gave the applicant a rough idea of the number of books that might be sold, and the amount of profit that might accrue to the applicant. This was certainly a rough estimate, and the subscription paid cannot be said to be commission paid by a seller to a wholesale purchaser. Subscription was paid when a school agreed to prescribe for its classes books of the applicant's publication. The payment was made before the actual starting of the business, *viz.*, the sale of books; furthermore, the actual number of books sold may be greatly different from (more or

(1) (1928) 3 I.T.C. 44.

less than) the number estimated by the applicant. We held that the payments of subscriptions were also made for *securing business*, and could not therefore be treated as allowable deductions from the profits of the business, just as the payments to Messrs. Feroze Din & Sons and Messrs. Attar Chand Kapoor & Sons were treated as inadmissible deductions, as explained in the preceding paragraph.

7. Maintenance allowance was paid to the applicant's mother. We mentioned the word "mother" in our appellate order. The payment was made really to the mother and the step-mother. This maintenance allowance was paid under certain awards of arbitrators. The allowance was disallowed in the assessments by the Income-tax authorities, and also by us in the second appeal before us. In our order under Section 33 we mentioned that a similar question arose in the assessment of a brother (Lala Hira Lal) of the *karta* of the Hindu undivided family who is the applicant before us now, and that the matter was pending before their Lordships of the Lahore High Court (66 R. A. No. Punjab, 1941-42). The facts and circumstances connected with the maintenance allowance in that other case and in the present case are exactly the same. Following the decision of the Bench of the Tribunal in Lala Hira Lal's appeal, we overruled the claim of the present appellant also. Their Lordships of the Lahore High Court, however, in Civil Reference case No. 22 of 1941 have decided the reference in *Lala Hira Lal's case*[1] in favour of the assessee by their order, dated 23rd March 1944. Both the applicant and the respondent say that a detailed statement of the case now is really not called for, inasmuch as the decision of their Lordships in *Lala Hira Lal's case*[1] will govern the point in the applicant's case also. We do not, therefore, give further details of the point here but in any case, we are bound to refer the question of law to the High Court again, as we have no power under the Act to give any direction to the Income-tax authorities without the specific decision of their Lordships in the references under consideration, to apply the decision in *Lala Hira Lal's case*[1] to the applicant's assessments for the four years we are now concerned with. We accordingly propose to refer to the Honourable High Court practically the same question as was referred to it in the statement of case in *Lala Hira Lal's case*[1] quoted above.

8. The questions formulated for reference to the High Court are :—

(1) Whether there is material for the finding that there is no genuine partnership ?

(2) Whether the expenditure is not deductible under Section 10 (2) (xii) as amended by Income-tax Act of 1939 ?

(1) Since reported in [1945] (13 I.T.R. 512).

(3) Whether in the circumstances the subscription paid to schools is not a legal charge on the revenue?

(4) Whether the mother is still a member of Hindu undivided family?

(5) Whether the maintenance allowance paid to her pursuant to the award is chargeable to tax in the hands of the applicant?

9. So far as questions one and two are concerned, Mr. Kirpa Ram Bajaj, who represented the applicant at the hearing of the application for reference, conceded that they were not fit to be referred as they were. He suggested that one question in place of these two questions might be formulated by us and referred to the Honourable High Court. In our view the following question may be framed :—

"Whether in the circumstances of the case, the payments made to (a) Messrs. Feroze Din & Sons and (b) Messrs. Attar Chand Kapoor & Sons were expenditure (not being in the nature of capital expenditure) laid out wholly and exclusively for the purpose of the business, and as such allowable under Section 10 (2) (xii) of the Income-tax Act?"

As already indicated, the question requires a slight modification, so far as the 1938-39 assessment is concerned. Having regard to the corresponding section of the Act before its amendment in 1939, the modified question for the 1938-39 assessment may be as below :—

"Whether in the circumstances of the case, the payments made to (a) Messrs. Feroze Din & Sons and (b) Messrs. Attar Chand Kapoor & Sons were expenditure (not being in the nature of capital expenditure) incurred solely for purposes of earning profits and gains of the business, and as such allowable under Section 10 (2) (ix) of the Income-tax Act before its amendment in 1939?"

10. In regard to the third question framed by the applicant, the wording of the question may be as follows :—

"Whether in the circumstances of the case, the subscriptions paid to certain schools were expenditure (not being in the nature of capital expenditure) laid out wholly and exclusively for the purpose of business, and as such allowable under Section 10 (2) (xii) of the Income-tax Act?"

For reasons already mentioned, the question in regard to the 1938-39 assessment needs a slight modification. The modified question may be :

"Whether in the circumstances of the case, the subscriptions paid to certain schools were expenditure (not being in the nature of capital expenditure) incurred solely for purposes of earning profits and gains of the business, and as such allowable under Section 10 (2) (ix) of the Income-tax Act before its amendment in 1939?"

11. Regarding questions Nos. (4) and (5) about maintenance allowance, for reasons mentioned above, we are referring this question in the same form in which it was referred to the High Court in *Lala Hira Lal's case*[1]. (The question was decided by their Lordships in Civil Reference Case No. 22 of 1941):—

"Whether in computing the assessable income of the assessee the amount paid by the assessee to the mother and the step-mother of the *karta* of the assessee Hindu undivided family in discharge of the liability to pay them maintenance under the awards dated 11th July 1936 and 17th December 1937 should be excluded?"

12. We, therefore, refer for the decision of their Lordships of the Lahore High Court the following questions of law :—

Regarding the assessment for the year 1938-39—

[66 R. A. No. 6 (Punjab) of 1944-45].

(1) Whether in the circumstances of the case the payments made to (a) Messrs. Feroze Din & Sons and (b) Messrs. Attar Chand Kapoor & Sons were expenditure (not being in the nature of capital expenditure) incurred solely for the purpose of earning profits and gains of the business, and as such allowable under Section 10 (2) (ix) of the Income-tax Act before its amendment in 1939?

(2) Whether in the circumstances of the case the subscriptions paid to certain schools were expenditure (not being in the nature of capital expenditure) incurred solely for the purpose of earning profits and gains of the business, and as such allowable under Section 10 (2) (ix) of the Income-tax Act before its amendment in 1939?

Regarding the assessments for the years 1939-40, 1940-41 and 1941-42—

[66 R. A. No. 7 (Punjab) of 1944-45.
66 R. A. No. 8 (Punjab) of 1944-45.
66 R. A. No. 9 (Punjab) of 1944-45].

(1) Whether in the circumstances of the case the payments made to (a) Messrs. Feroze Din & Sons and (b) Messrs. Attar Chand Kapoor & Sons were expenditure (not being in the nature of capital expenditure) laid out wholly and exclusively for the purpose of business, and as such allowable under Section 10 (2) (xii) of the Income-tax Act?

(2) Whether in the circumstances of the case the subscriptions paid to certain schools were expenditure (not being in the nature of capital expenditure) laid out wholly and exclusively for the purpose of business, and as such allowable under Section 10 (2) (xii) of the Income-tax Act?

Regarding the assessments for the years 1938-39, 1939-40, 1940-41 and 1941-42—

(1) (1945) 13 I.T.R. 512.

[66 R. A. No. 6 (Punjab) of 1944-45.
66 R. A. No. 7 (Punjab) of 1944-45.
66 R. A. No. 8 (Punjab) of 1944-45.
66 R. A. No. 9 (Punjab) of 1944-45].

(3) Whether in computing the assessable income of the assessee the amount paid by the assessee to the mother and step-mother of the *karta* of the assessee Hindu undivided family in discharge of the liability to pay them maintenance under the awards dated 11th July 1936 and 17th December 1937 should be excluded?

Kirpa Ram Bajaj and *Narendar Nath Chopra*, for the assessee.
S. M. Sikri and *Jindra Lal*, for the Commissioner.

JUDGMENT.

MEHR CHAND MAHAJAN, J.—For the years 1938-39, 1930-40, 1940-41 and 1941-42, assessments to income-tax were made on the firm R.S. Munshi Gulab Singh and Sons, Lahore, in respect of the income derived by it from business. On appeal these assessments were confirmed by the Appellate Assistant Commissioner of Income-tax. The assessee firm went up in second appeal to the Income-tax Tribunal, Allahabad. The Tribunal allowed partial relief to the assessee but did not allow all the deductions claimed by it. The assessee thereupon under Section 66 (1) of the Income-tax Act required the Tribunal to refer to this Court certain questions of law arising with regard to the validity of the assessments. The Tribunal accordingly drafted one consolidated statement of the case in respect of all the four assessments and referred for the decision of this Court the following questions of law:—

(1) Whether in the circumstances of the case the payments made to (a) Messrs. Feroze Din and Sons and (b) Messrs. Uttar Chand Kapur and Sons were expenditure (not being in the nature of capital expenditure) incurred solely for the purpose of earning profits and gains of the business, and as such allowable under Section 10 (2) (ix) of the Income-tax Act before its amendment in 1939?

(2) Whether in the circumstances of the case the subscriptions paid to certain schools were expenditure (not being in the nature of capital expenditure) incurred solely for the purpose of earning profits and gains of the business and as such allowable under Section 10 (2) (ix) of the Income-tax Act before its amendment in 1939?

These two questions concern the assessment for the year 1938-89.

(3) Whether in the circumstances of the case the payments made to (a) Messrs. Feroze Din and Sons and (b) Messrs. Uttar Chand Kapur and Sons were expenditure (not being in the nature of capital expenditure) laid out wholly and exclusively for the purpose of business, and as such allowable under Section 10 (2) (xii) of the Income-tax Act,

(4) Whether in the circumstances of the case the subscriptions paid to certain schools were expenditure (not being in the nature of capital expenditure) laid out wholly and exclusively for the purpose of business, and as such allowable under Section 10 (2) (xii) of the Income-tax Act.

It may be observed that the nature of the payments involved in questions 1, 2, 3 and 4 is the same. But separate questions have to be framed in respect of the year 1938-39 owing to amendments made in the Act in the year 1939.

(5) Whether in computing the assessable income of the assessee the amount paid by the assessee to the mother and step-mother of the *karta* of the assessee Hindu undivided family in discharge of the liability to pay them maintenance under the awards dated the 11th July, 1936, and 17th December, 1937, should be excluded.

It is necessary to set out in some detail the material facts. The firm of Messrs. R. S. Munshi Gulab Singh and Sons is a Hindu undivided family firm. Rai Bahadur Sohan Lal and his sons as members of an undivided family own the firm. Their concern is of printers and publishers. The printing press was established by R. S. Munshi Gulab Singh, grandfather and great grandfather of the members of the coparcenary. It is not a business started or acquired by the *karta* of the assessee joint family and he has incurred no expenditure in acquiring the concern. The printing press owned by the assessee firm is one of the biggest in the town of Lahore. Messrs. Feroze Din and Sons and Messrs. Uttar Chand Kapur and Sons respectively are owners of printing presses and carry on the business of printers and publishers. They are competitors of the assessee in this trade. The capacity of the printing press of the assessee is greater than the printing capacity of the presses owned by these two firms. Consequently the establishment and other expenses of the assessee are appreciably more than those of his competitors so that these two concerns could charge comparatively low rates for printing work and yet make profits which was not possible for the assessee to do. In order, therefore, to secure full time work for his press and in the interests of his business the assessee arrived at an arrangement with his competitors and persuaded them to quote uniform rates with the assessee in the various tenders given to obtain Government orders for printing and publishing work, in other words a tripartite arrangement was arrived at by which the parties agreed not to underbid each other. Under this arrangement the assessee agreed to pay to his competitors certain sums of money. These payments were in the shape of a share in the estimated profits of the assessee in working the orders thus secured from

Government. The estimate of profits was arrived at by deducting certain agreed cost contemplated to be incurred in the execution of the job from the amount of tendered price. This estimate did not take into consideration the actual profits that may be earned or realised by the assessee or the possible loss that may accrue to him. The compensation was of course payable when Government paid the bills. Counsel for the assessee gave these material facts to the Tribunal and the Tribunal accepted these facts and made the reference on the assumption that they were correct. The same learned counsel during the course of his arguments explained the precise situation to us. It was said at the Bar that the agreement was of a reciprocal nature. In case the competing firms obtained orders from Government at the agreed rates and executed the work which otherwise the assessee might have done they also paid a share to the assessee in the estimated profits arrived at as above indicated. The profits respectively obtained by the assessee or by the competing firms under this arrangement were included in the profit and loss account of the various firms and were consequently taxed under the Act. It was said that the arrangement was an oral one. In respect to the year 1940-41 in the matter of one piece of work a written arrangement was also arrived at between the parties. This writing was produced before the Tribunal and was also shown to the Income-tax Officer and we had the benefit of perusing it. Learned counsel said that the terms contained in this writing were substantially the terms of the oral arrangement set up by him before the Tribunal. It is these payments made under this arrangement by the assessee to his competitors that were claimed by him as allowable deductions under the provisions of Section 10 (2) (ix) of the old Act and Section 10 (2) (xii) of the new Act.

The Income-tax Officer regarded these payments as a hush money paid to satisfy the rival concerns and to dissuade them from competing with the assessee firm. He, therefore, held that hush money paid to the rival firms could not be allowed as a deduction under either of the above provisions. The Assistant Commissioner of Income-tax affirmed this view. The Appellate Income-tax Tribunal however, reached the conclusion that having regard to the nature of these payments it must be said that they were incurred to shut out competition with a view to secure business which would enable the assessee to earn profits or to earn more profits than could otherwise be earned. Having arrived at this conclusion as to the nature of the payments made to the two concerns it was held that it could not by any stretch of imagination be said that the expenditure in question was incurred solely for the purpose of earning such profits and

gains or was laid out wholly and exclusively for the purpose of such business—it was clearly incurred for securing business as distinguished from carrying on business or earning profit from it. For this view reliance was placed on a decision of the Madras High Court in the case of *Rao Saheb A. S. Alaganan Chetty* v. *Commissioner of Income-tax, Madras*[1]. Questions 1 and 3 referred to us relate to these payments and arise out of this decision.

The facts giving rise to questions 2 and 4 are simple. The assessee paid certain amounts by way of subscription to various schools which agreed to prescribe for their classes school books published by it. The amount of subscription to each school was calculated after taking into consideration the number of boys in each class for which the firm's books would be prescribed. This mode of calculation furnished the assessee with a rough idea of the number of books that might be sold and the amount of profit likely to be earned. It was claimed by the assessee that the expenditure thus incurred was an allowable deduction as a legitimate business expenditure as it had been incurred in the interests of business and fell within the ambit of Section 10 (2) (ix) of the old Act and Section 10 (2) (xii) of the new Act.

The Income-tax Officer and the Assistant Commissioner of Income-tax disallowed this claim on the ground that voluntary subscription paid was not in the nature of a commission on sale of books and was thus not a legitimate business deduction. The Tribunal, however, reached the conclusion that the payment was not in the nature of a voluntary subscription but was made with an end in view. It was clearly the securing of business, *viz.*, of sale of books and thus being expenditure incurred in securing a business and not in carrying on the business was not allowable under either of the above provisions contained in Section 10 of the Act.

The matter covered by question No. 5 concerns the maintenance allowance paid to the mother and the step-mother of Rai Bahadur Sohan Lal. Rai Bahadur Mohan Lal left him surviving five sons, two widows and some grandsons. In the year 1936 Rai Bahadur Sohan Lal the *karta* of the assessee family partitioned the family estate with his brothers and disrupted. The partition award directed the four brothers to pay a sum of Rs. 400 a month to their mother and Rs. 200 a month to the step-mother and made the amount of the maintenance a charge on some property. The maintenance was raised to Rs. 450 on the death of one of the brothers by an award and was similarly made a charge on some property. It was held by the Income-tax authorities and the Tribunal that after disruption the

(1) (1928) 3 I.T.C. 44.

mother's status as a member of the family was not affected and she remained joint with all the groups into which the family had been split up. Consequently any amount received by her as maintenance from any group of the family was received by her as a member of a Hindu undivided family on which no tax is payable under the law and that being so such amounts could not be excluded in assessing the income of the newly constituted group of the family. The result was that the deduction claimed was disallowed.

It will be convenient to deal with the fifth question first as it requires no discussion on my part. This very identical question arose in the case of assessment of Hira Lal, brother of Rai Bahadur Sohan Lal in C. R. 22 of 1941 and was decided by a Bench of this Court on the 23rd March, 1944 [1]. My learned brother was a party to that decision which was in these terms :—

"In the present case it is clear that by reason of the awards in 1936 and 1937, by which the maintenance allowance payable to the widows was made a charge on the property of the brothers, which awards were duly made a rule of Court and decreed as such, the payments to the widows are obligatory and subject to an overriding charge. It follows, therefore, that the payments made by the assessee in discharge of his share of the liability should not be taxed as income in the hands of the assessee Lala Hira Lal but must be excluded from his assessable income. Accordingly the question formulated by the Income-tax Tribunal must be answered in the affirmative."

For the reasons given by the Division Bench in the above mentioned case question No. 5 is answered in the affirmative. It may be observed that the learned counsel for the Commissioner of Income-tax did not challenge the correctness of the decision in C. R. 22 of 1941 before us and conceded that the answer to question No. 5 be given in the affirmative.

In order to find a satisfactory solution to the problems stated in questions 1 and 3 it is necessary to cite the relevant provisions of the Act under which the expenditure incurred is claimed as deduction. Section 10 (2) (ix) of the old Act is in these terms :—

"10 (1) The tax shall be payable by an assessee under the head "Business" in respect of the profits or gains of any business carried on by him.

(2) Such profits or gains shall be computed after making the following allowances, namely :—

* * * * *

(ix) any expenditure (not being in the nature of capital expenditure) incurred solely for the purposes of earning such profits or gains."

(1) Since reported as *Hira Lal, In re* [1945] 13 I.T.R. 512.

After amendment of the Act in 1939 clause (xii) was substituted for clause (ix) which reads as follows:—

"(xii) Any expenditure (not being in the nature of capital expenditure or personal expenses of the assessee) laid out or expended wholly and exclusively for the purposes of such business, profession or vocation."

The amended Act has brought the law in India in respect of business allowances in conformity with the English Act.

The point for consideration and decision on these two questions, therefore, is whether the amounts paid to Messrs. Feroze Din and Sons and Messrs. Uttar Chand Kapur and Sons could pass under the harrow of either the old clause (ix) or new clause (xii) of Section 10, sub-section (2), of the Act. Could it be said that the expenditure incurred by means of these payments was either incurred solely for the purpose of earning the profits and gains and was not capital expenditure or that the expenditure laid out was expended wholly and exclusively for the purpose of such business.

To answer these two questions it is essential to determine the exact nature of this expenditure and the true nature of the concern run by the assessee. As already stated the assessee is the owner of an ancestral printing press. In order to keep the press going the assessee firm has to secure work so that it may show a substantial turnover and thus earn profits after meeting the expenses of establishment and other costs incidental to the trade. The assessee firm is not merely a firm of contractors but is the owner of an established ancestral trade which it has inherited. Customers place orders with the firm for printing and publishing jobs. These orders either come unsolicited or are canvassed. In case of Government jobs tenders have to be submitted to get printing and publication work. After the work is secured in this manner it is executed at the press and prices are realised for the printing work and from sale of the books published at the press. The method of calculation of profits is the usual commercial method, that is the cost incurred in finishing the printing and publication jobs is deducted out of the price received, that is out of the amount received from the customer for work done. In this situation and in a concern of this nature point arises whether payments made to secure work orders or to secure more work than would otherwise come are in the nature of capital or revenue expenditure. There can be no question but that the payments are made to shut out competition with a view to secure work which would enable the assessee to earn profits or to earn more profits than could otherwise be earned. This is the finding at which the Tribunal has arrived in regard to the purpose and object of these payments.

The Tribunal has, however, employed the expression "securing business" in a wider and a popular sense as synonymous with the phrase "securing any job or piece of work for the press." That, in my opinion, was not an apposite expression in the facts and circumstances of the present case. All that could be said was that the assessee in order to carry on his business of the printing press was by incurring this expenditure getting work to run his press to its full capacity and to his maximum advantage, but it could not be said that he was acquiring a new business or in other words was incurring this expenditure to acquire a concern. In this connection reference may be made to a few leading cases. The classical observations of Bowen, L.J., in *The City of London Contract Corporation* v. *Styles*[1] may be cited with advantage on the subject. About capital his Lordship said:—

"You do not use it 'for the purpose of' your concern, which means, for the purpose of carrying on your concern, but you use it to acquire the concern."

It is not possible to say in the present case that the sums in question were used to acquire the printing press or the ancestral business of the assessee. There is no justification for the suggestion that each individual printing contract obtained by the assessee's concern or any expenditure incurred to get an item of work for the press is an amount spent to acquire the concern. To carry on the business of a printing press it is necessary to canvass work for it by giving tenders or otherwise. The expenditure incurred in canvassing custom or in securing better rates than otherwise would be obtainable for the work executed in this concern with the object of earning increased profits is not capital expenditure. According to the ordinary commercial usage and mode of drawing up a profit and loss account it would usually be debited to the revenue account.

In *The City of London Contract Corporation* v. *Styles*[1] a running business, that is a going concern under the style and name of Charles Phillips and Co., contractors and engineers and their contracts, plant and materials, etc., were acquired by the appellant in that case. A part of the sum paid towards the acquisition of those contracts was debited to revenue account. It was held that the price paid for such contracts was not a deduction from the profits arising from their performance. Esher, M. R., in this case observed as follows:—

"There is an endeavour to carry us so far as to go into the description of the business, and to say that the £1,80,000 is not capital because of the description of the business, but if they *bought* the business, whatever it may be, and whatever it consisted of, the fact that it

(1) (1887) 2 Tax Cas. 239, at p. 243.

is the capital which they embarked in that business cannot be doubted. Now if that was the capital which they embarked in that business, they then proceeded to carry on the business. How can you carry on a business after you have embarked your capital in the *purchase* of it? You must find new money in order to pay the expenses year by year, but then you do find money to pay the expenses year by year, and you get the receipts year by year, and the difference between the expenses necessary to earn the receipts of the year and the receipts of the year are the profits of the business for the purpose of the income tax."

In my opinion the expenditure incurred in the present case is in the nature of an annual business expense incurred to run the press to its full capacity and to earn the maximum amount of profit. No part of it can be said to have been embarked to purchase the business. The sums paid to competing firms to tender the same rates as tendered by the assessee are paid with the sole purpose and object of earning substantial profits in running the printing press business. The whole object of this payment is to tender rates for work that bring in lucrative profits.

Learned counsel for the petitioner firm cited the case of *Guest, Keen and Nettlefolds* v. *Fowler*[1], and argued that the rule laid down in that case furnished a good guide for the decision of the present case. In that case the Steel Hoop Manufacturers' Association was founded for the purpose of keeping up prices and thus earning larger profits by its members agreeing to adhere to fixed prices and thereby preventing competition among themselves. The members were entitled to shares of the total orders received by the whole of the members in certain agreed proportions. If any member invoiced more than the proper percentage, a fixed amount of 10 s. per ton on the excess had to be paid by that member to the Association which distributed that payment in due proportion amongst those members who had invoiced less than their proportionate quantities. The assessment was made on Messrs. Guest, Keen and Nettlefolds Ltd., for the year 1907-8 under Schedule D of the Income Tax Acts and an item of £316-6s. was included in it on account of the payment made by them to the Steel Hoop Manufacturers' Association of which they were members. The question for the opinion of the Court was whether the payments made to the Association were a proper deduction to be made in arriving at the amount for assessment. It was argued in that case that the payments to the Association were made out of profits with a view to earning profits and the members keep up the prices by the arrangement and so were enabled to earn profits they had in fact earned.

(1) (1910) 5 Tax Cas. 511.

It was also suggested that the other firms which received payments from the pool would pay tax on those payments as part of their profits. Bray, J., gave the following opinion in that case :—

" What I have to find is, and I cannot find for the appellants unless I am satisfied, that that is money wholly or exclusively laid out or expended for the purposes of such trade. Now what is the trade? The trade of the appellants is the manufacture and sale of certain goods, steel hoops. What are the main operations of that trade? First the steel hoops have to be made; secondly they have to be sold; and, as has been pointed out in more than one case, the trade includes not only the manufacture but the selling; and indeed the selling is very often the most important part; the whole of the profits depends upon the price. What does the selling consist of? It consists of two things: the finding of the customer and making a bargain with the customer as to the price, the object being of course to get the highest possible price. I do not think this arrangement that is made between the three firms has anything to do with finding the customer. I think it all relates to the fixing of the price, and it is obvious that if the appellants can make an arrangement with their competitors that their competitors will not sell below a certain price, they will be able, or may be able at all events, to get that price or a higher price for their goods. That is part of the business part of the trade they are carrying on, to get the highest price they can for their goods. What I have to see is whether this money which was expended was wholly laid out or expended for that purpose; that is for the purpose of selling their goods at the greatest possible advantage......" The " Association is mainly formed for the purpose of keeping up prices and thus earning larger profits."......There was no other object whatever of the Association and, " therefore it seems to me I am bound to find that this money was paid for the purpose of keeping up the price and thus earning the larger profits of the trade " and thus the money was " wholly or exclusively laid out or expended for the purposes of such trade. "

I am in agreement with the suggestion of the learned counsel that the opinion expressed by Bray, J., in the above-mentioned case furnishes a guide for deciding the present case. The sums were paid to the competing firms by the assessee in order to keep up prices for the printing and publishing jobs executed at the press and thus earn larger profits than could otherwise be realised. This is part of the business part of the trade that the assessee carries on as the owner of a printing press and as a person who has inherited the trade of a printer and publisher. My answer, therefore, to questions 1 and 3 is in the affirmative.

Mr. Sikri, learned counsel for the Commissioner of Income-tax, in the first instance raised a preliminary point. He contended that there was no material before the Tribunal on the basis of which questions 1 and 3 could be referred to this Court and that the assumption in the statement of the case by the Tribunal as to the nature of the expenditure was not justified. In my opinion this contention is without force. The functions of this Court in a reference made under Section 66 (1) of the Income-tax Act are stated in Section 66 (5) of the Act. The questions referred on the statement of case made by the Tribunal have to be answered unless they are of an academic nature. It is the duty of the Tribunal to state the facts and to formulate the questions. If I may say so, it is for the Tribunal to find facts and it is for this Court to lay down the law applicable to facts found. As I have already stated, if on facts stated no question of law arises or the question that arises is purely of an academic nature then this Court is not bound to answer the question referred.

Further I am of the opinion that the point raised by Mr. Sikri cannot be sustained for the simple reason that there was material before the Tribunal and this material warranted the reference and the questions submitted to this Court. Learned counsel for the assessee stated at the Bar the facts as to the nature of the payments made to Messrs. Feroze Din and Sons and Messrs. Uttar Chand Kapur and Sons. The statement made at the Bar was accepted by the Tribunal and no challenge on its correctness was thrown on behalf of the counsel appearing for the Commissioner of Income-tax. In these circumstances there is no justification for the contention that there was no material before the Tribunal to determine the precise nature of these payments and the reference, therefore, is based on hypothetical grounds. For the reasons given above, the preliminary point cannot be sustained.

On the merits of the case Mr. Sikri raised several contentions in the alternative. Firstly, he argued that these payments were in the nature of capital expenditure and that they had been made to secure the business of the assessee. According to the learned counsel each printing or publishing job or a work order obtained by the assessee as a printer and publisher amounted to the acquisition of a new business and that being so the expenditure incurred for the acquiring of work was not incurred to carry on the business and was capital expenditure. I have sufficiently dealt with this matter in the earlier portion of this judgment. In my view the argument of the learned counsel is based on a wrong apprehension as to the true nature of the assessee's concern. For this contention learned counsel made reference

to the case of *Rao Saheb A. S. Alaganan Chetty* v. *Commissioner of Income-tax, Madras*[1]. In that case the assessee was doing business as a carrying contractor. He paid the sum of Rs. 12,000 to the rival contractor to induce the latter not to compete with him. As a result of the non-competition of his rival he obtained the carrying contract at a rate higher than the previous year's rate enabling him to make larger profits. On an assessment to income-tax, the aforesaid sum was claimed as a deduction in the computation of his taxable profits under Section 10 (2) (ix) of the Act. It was held that the payment of this sum not being for the purpose of working the contract but for obtaining it, was capital expenditure and not a permissible allowance under Section 10 (2) (ix) of the Act. The learned Chief Justice who delivered the judgment of the Special Bench in the concluding portion of his judgment made the following observations:—

"What is the position here? Applying the one which, to my mind, is the easiest to apply, Bowen, L. J.'s test, surely any plain man would say that this money was paid not for the purpose of working the contract but of getting it at all; it was the price that had to be paid to obtain the contract."

It is obvious that the learned Chief Justice regarded the amount paid as an expenditure incurred for the acquisition of a new concern and considered that each contract obtained in that case was a new business acquired by the assessee. In the present case I have already found that this is not so and that each item of work is not a new business acquired by the assessee every time. That being so, that case is of no assistance in deciding the present case. If that case is considered an authority for the proposition that in an established ancestral business carried on by an assessee if he takes a piece of work on the foot of a contract and incurs expenditure for obtaining that contract, such expenditure is capital expenditure, then with great respect I express my dissent from that view. It is not possible for me to subscribe to the proposition that in the business of a printing press every time that contracts are made with customers to obtain printing or publication work from them such contracts amount to a new business and the expenditure incurred in obtaining those contracts is in the nature of capital expenditure.

Reliance was also placed on the decision of their Lordships of the Privy Council in *Tata Hydro Electric Agencies Ltd., Bombay* v. *Commissioner of Income-tax, Bombay*[2]. In that case it was held that where an obligation to make payments is undertaken in consideration of the acquisition of the right to earn profits, that is of the right to conduct

(1) (1928) 3 I.T.C. 44. (2) (1937) I.L.R. 1937 Bom. 388; 5 I.T.R. 202.

the business, and not for the purpose of producing profits in the conduct of the business, the payments cannot be deducted in estimating the profits of the business under Section 10 (2) (ix) of the Indian Income-tax Act, 1922. There an agreement had been arrived at between the Tata Power Co., Ltd., and Tata and Sons Ltd., under which Tata and Sons Ltd., were appointed managing agents of Tata Power Co., Ltd., for 41 years on terms that they should receive a commission of 10 per cent. on the net profits of the company, subject to a minimum of Rs. 50,000, whether the company made any profits or not, and other allowances. The agency was assignable. Tata Sons Ltd., also entered into agreements with two persons under which these two persons lent money to Tata Power Ltd., on terms that, in addition to interest, they were each to receive under their respective agreements 2 annas in the rupee in all the commission and remuneration earned by Tata Sons Ltd., under their agreement with Tata Power Co., Ltd. Tata Sons Ltd., assigned their rights and interests to the Tata Hydro-Electric Agencies Ltd., subject to their obligations to the two creditors for a cash consideration and shares of certain value. After the acquisition of the agency business by the Tata Hydro-Electric Agencies Ltd., a direct arrangement was also arrived at between them and the Tata Power Co., Ltd. They thus became completely substituted in place of Tata and Sons Ltd., in all respects both as regards the right to receive from the Tata Power Co., Ltd., the stipulated agency remuneration and as regards the obligation to pay out of that remuneration 12½ per cent. to F. E. Dinshaw Limited and 12½ per cent. to Richard Tilden Smith's administrator. In the year 1932 the managing agents duly earned and received payment from the Tata Power Company of their commission of 10 per cent. on the net profits of that company and duly paid over to F. E. Dinshaw Limited and to Richard Tilden Smith's administrator 12½ per cent. thereof each, or 25 per cent. in all. The assessment of the appellants' income for tax purposes for the fiscal year to March 31, 1934, was based on their income, profits and gains for the year 1932 and the question was whether in the computation for tax purposes of their income, profits and gains for that year they were entitled to deduct a sum representing the 25 per cent of the commission earned and received from the Tata Power Company Ltd. which they paid over to F. E. Dinshaw Limited and Richard Tilden Smith's administrator. On these facts their Lordships made the following observations:—

"It was not questioned by counsel for the Crown that, if the present question had arisen with Tata Sons Ltd., they would, under Section 10 (2) (ix), have been entitled on the facts stated to deduct

their payments to F. E. Dinshaw Limited and Richard Tilden Smith as being expenditure incurred solely for the purpose of earning their profits or gains. But he submitted that after the acquisition of the agency business by the present appellants the payments assumed a different character. The appellants, he said, did not take any part in obtaining the loans nor did they incur the liabilities in question in the course of rendering any services to their principals. The obligation to make the payments in question was taken over by them as part of the transaction whereby they acquired the agency business from Tata Sons Ltd. and the payments were, therefore, made not for the purpose of earning profits in the conduct of the agency business but in fulfilment of the terms on which they purchased the business.

Their Lordships recognise and the decided cases show how difficult it is to discriminate between expenditure which is, and expenditure which is not, incurred solely for the purpose of earning profits or gains. In the present case their Lordships have reached the conclusion that the payments in question were not expenditure so incurred by the appellants. They were certainly not made in the process of earning their profits; they were not payments to creditors for goods supplied or services rendered to the appellants in their business; they did not arise out of any transactions in the conduct of their business. That they had to make those payments no doubt affected the ultimate yield in money to them from their business but that is not the statutory criterion. They must have taken this liability into account when they agreed to take over the business. In short, the obligation to make these payments was undertaken by the appellants in consideration of their acquisition of the right and opportunity to earn profits, that is, of the right to conduct the business, and not for the purpose of producing profits in the conduct of the business. If the purchaser of a business undertakes to the vendor as one of the terms of the purchase that he will pay a sum annually to a third party, irrespective of whether the business yields any profits or not, it would be difficult to say that the annual payments were made solely for the purpose of earning the profits of the business."

It is clear that in the case before their Lordships of the Privy Council the expenditure had been incurred for acquiring the concern and not for running the concern and that being so it was in the nature of capital expenditure. The *ratio decidendi* of that case has no application to the facts of the present case.

Mr. Sikri also referred to a decision of the House of Lords in *Atherton* v. *British Insulated and Helsby Cables, Limited*[1].

(1) (1925) 10 Tax Cas. 155.

He particularly placed reliance on certain observations in the speech of Viscount Cave, L.C., at page 192 of the report:—

"But there remains the question, which I have found more difficult, whether apart from the express prohibitions, the sum in question is (in the words used by Lord Sumner in *Usher's case*[1]) a proper debit item to be charged against incomings of the trade when computing the profits of it; or, in other words, whether it is in substance a revenue or a capital expenditure. This appears to me to be a question of fact which is proper to be decided by the Commissioners upon the evidence brought before them in each case; but where, as in the present case, there is no express finding by the Commissioners upon the point, it must be determined by the Courts upon the materials which are available and with due regard to the principles which have been laid down in the authorities. Now, in *Vallambrosa Rubber Company* v. *Farmer*[2], Lord Dunedin, as Lord President of the Court of Session, expressed the opinion that 'in a rough way' it was 'not a bad criterion of what is capital expenditure as against what is income expenditure to say that capital expenditure is a thing that is going to be spent once and for all and income expenditure is a thing which is going to recur every year'; and no doubt this is often a material consideration. But the criterion suggested is not, and was obviously not intended by Lord Dunedin to be, a decisive one in every case; for it is easy to imagine many cases in which a payment, though made 'once and for all,' would be properly chargeable against the receipts for the year. Instances of such payments may be found in the gratuity of £ 1,500 paid to a reporter on his retirement which was the subject of the decision in *Smith* v. *Incorporated Council of Law Reporting*[3], and in the expenditure of £4,994 in the purchase of an annuity for the benefit of an actuary who had retired which, in *Hancock* v. *General Reversionary and Investment Company*[4], was allowed, and I think rightly allowed, to be deducted from profits. But when an expenditure is made, not only once and for all, but with a view to bringing into existence an asset or an advantage for the enduring benefit of a trade, I think that there is very good reason (in the absence of special circumstances leading to an opposite conclusion) for treating such an expenditure as properly attributable not to revenue but to capital. For this view there is already considerable authority. Thus, moneys expended by a brewing firm with a view to the acquisition of new licensed premises (*Southwell* v. *Savill Brothers*[5]); 'fitting expenses' incurred in transferring a

(1) (1914) 6 Tax Cas. 399.
(2) (1910) 5 Tax Cas. 529.
(3) [1914] 3 K.B. 674.
(4) [1919] 1 K.B. 25.
(5) [1901] 2 K. B. 349.

manufacturing business to new premises (*Granite Supply Association* v. *Kitton*[1]); costs incurred in promoting a Bill which was dropped on the desired facilities being obtained by agreement (*A. G. Moore and Company* v. *Hare*[2]); and expenditure incurred by a shipbuilding firm in deepening a channel and creating a deep water berth (not on their own property) to enable vessels constructed by them to put out to sea (*Ounsworth* v. *Vickers*[3]) have been held to be in the nature of capital expenditure and not to be deductible under the Income Tax Acts; and *Rowntree and Company* v. *Curtis*[4] is to the same effect. I think that the principle to be deduced from this series of authorities rests on sound foundations and may properly be adopted by this House."

The payment under discussion in that case was made not merely as a gift or bonus to the older servants of the appellant company, but to "form a nucleus" of the Pension Fund which it was desired to create, and contributions made to that fund were sought to be deducted as a business deduction. The observations of Viscount Cave, L. C., lend considerable support to the view that I have expressed about the expenditure in question in this case. The expenditure is not made once and for all or with a view to bring into existence an asset or an advantage for the enduring benefit of the trade. This expenditure is incurred during the course of the year when certain contracts for printing and publication jobs for the printing press have to be taken from Government on the basis of tenders submitted to it. The expenditure is of a recurring nature and arises in the course of the trade and confers no enduring benefit on the trade. It only enhances the annual profits and has no other purpose or object in view. In these circumstances I cannot subscribe to the contention of Mr. Sikri that this expenditure was either in the nature of a capital expenditure or was such as conferred an enduring advantage on the trade. Mr. Sikri also mentioned the case of *Collins* v. *Joseph Adamson and Company*[5]. In that case the taxpayer was a member of an Association of boiler-makers having for its object the maintenance of prices by means of a pooling system. The Association, in order to secure the success of its object, purchased the undertaking of a company which was a member of the Association in order to close it down and prevent its being purchased by persons outside the Association. It also made a grant to one of its members to enable that member to acquire a controlling interest in an outside competing business and bring its operations within the rules of the Association. The taxpayer sought to deduct from his

(1) (1905) 5 Tax Cas. 168.
(2) [1914] 6 Tax Cas. 572.
(3) [1915] 3 K. B. 267.
(4) [1925] 1 K. B. 328.
(5) [1938] 1 K. B. 477; 7 I.T.R. 92.

trading profits for the purpose of income-tax assessment his share of the Association's expenses in each instance and it was held that in each instance the payment made by the Association had created for the members of the Association advantages of an enduring nature properly to be treated as capital, and in neither case was the deduction which was claimed allowable. That case again is distinguishable from the present on the ground that the expenditure incurred was incurred to purchase the undertaking of a competing company and the money spent was not used in the running of the business of the concern. Reference was also made to the case of *Stott* v. *Hoddinott*[1]. In that case the assessee carried on the business of architect, surveyor and engineer and in order to secure contracts for the erection of mills it became necessary for him to take up shares of the milling companies granting the contracts. These shares were subsequently sold at various dates at a loss and it was held that the loss was a loss of capital and was not an admissible deduction in arriving at appellant's profits for assessment. At page 91 of the report the following observations occur :—

"Now, it has to be remembered that what one is dealing with in this case is profits, and as I said in the last case, profits are to be ascertained according to ordinary commercial principles, except so far as you can find that those principles are modified or altered by the express words of the statute, and applying the rules which are laid down in the statute. I think it is quite plain that if, in fact, that which has been done is an investment in the nature of capital, and that the loss that has been suffered is a loss in the nature of a capital loss, then such a loss could not properly be deducted when you are estimating the annual profits or gains for a particular year."

Any amount invested in the purchase of shares could hardly be said to be expense incurred in carrying on a concern. It is plain to my mind that that case has no relevancy to the facts and circumstances of the present case. As I put it to the learned counsel and it has been observed in several cases that profits have to be ascertained according to ordinary commercial principles. In my view applying those ordinary commercial principles payments made in the present case fall in the category of revenue expenditure and cannot be considered as capital expenditure.

Secondly, Mr. Sikri contended that payments in the present case were made out of profits after they had been earned and, therefore, could not fall within the ambit of Section 10 (2) (ix) or (xii). The Tribunal found that the expenditure was in the nature of compensation paid to the rival firms for quoting the same prices as the assessee

(1) (1916) 7 Tax Cas. 85.

would quote and is not paid out of profits actually earned or after they have accrued. These payments were made on the basis of an artificial estimate of would be profits. The payment is actually made as soon as the customer pays the bill. It is not delayed till the time of the preparation of the profit and loss account of the total business of the assessee for the whole year. Instead of a lump sum for each job it is a sum which can be arithmetically arrived at on the figures of cost and price agreed upon between the parties. The actual profit and loss of the concern does not affect these payments. In these circumstances this contention of Mr. Sikri is also untenable. Mr. Sikri in this connection placed reliance on two cases. The first of these is a Privy Council decision in *Pondicherry Railway Co., Ltd.* v. *Commissioner of Income-tax, Madras*[1]. At page 370 of the report the rule laid down by Lord Chancellor Halsbury in *Gresham Life Assurance Society* v. *Styles*[2] was cited :—

"The thing to be taxed," said his Lordship, "is the amount of profits or gains. The word 'profits' I think is to be understood in its natural and proper sense—in a sense which no commercial man would misunderstand. But when once an individual or a company has in that proper sense ascertained what are the profits of his business or his trade, the destination of those profits or the charge which has been made on those profits by previous agreement or otherwise is perfectly immaterial. The tax is payable upon the profits realised and the meaning to my mind is rendered plain by the words 'payable out of profits.'"

As I have already observed the payment made to the competing firms is not made out of profits realised. There is no arrangement between the three competing firms that after ascertaining annual profits each will have a share out of those profits. That case again has no application here. The second case relied upon is the case of *Gopinath Vir Bhan* v. *Commissioner of Income-tax, Punjab*[3], a Bench decision of this Court, where the judgment was delivered by my learned brother. In that case the assessee had the advantage of securing a monopoly of ginning his own cotton. The assessee entered into an agreement with a company by which he agreed to get all the raw cotton purchased by him ginned by the company and the company agreed not to do ginning or pressing for any other customer. In addition to ginning charges at certain rates the assessee agreed to pay to the company as additional ginning charges one-third of the net profits earned by him in his cotton and seed business after deducting all expenses connected with the sale and purchase of cotton and seed. In

(1) (1931) 5 I. T. C. 363.
(2) (1892) 3 Tax Cas. 185.
(3) (1938) 6 I. T. R. 243.

the case of loss no sum was to be paid to the company nor was the company bound to make any contribution on that account. In the accounting year the assessee paid to the company Rs. 68,000 odd towards ginning charges and Rs. 22,429 towards one-third of the net profits in accordance with their agreement. On those facts it was held that the sum of Rs. 22,429 paid by the assessee to the company was not a legitimate deduction under Section 10 (2) (i) of the Indian Income-tax Act inasmuch as a fluctuating item like a share in the profits cannot be treated as rent within the meaning of Section 10 (2) (i); and also not deductible under Section 10 (2) (ix) as the payment was a payment out of the profits after they had been earned and not an expenditure incurred for earning the profits. The decision in that case followed the decision of their Lordships of the Privy Council in *Pondicherry Railway Co., Ltd.* v. *Commissioner of Income-tax, Madras*[1]. As already stated the rule laid down in those cases has no application to the facts and circumstances of the present case.

Lastly, Mr. Sikri urged that the true nature of the arrangement in the present case was that it was in the nature of a *quasi* partnership agreement and that the payment made by one partner to the other partners could not be held to be a legitimate business deduction. If Mr. Sikri was right in the construction of this arrangement there would be no question but that the payment could not be legitimately allowed. In my view, however, the construction placed on the agreement by Mr. Sikri cannot be accepted. Under this arrangement tenders are submitted to the Government for each piece of work by the competing firms by quoting identical rates but the work is executed by any one of the firms to whom it is eventually given by the Government. That firm executes the work and takes all the profit that accrues. In this profit the other firms have no share. For quoting identical rates in the tender a payment is made by the firm that obtains the work to the other firms on the basis of an artificial estimate. There is no partnership of any kind between the rival firms in the execution of the work or even in the ultimate profit and loss of that venture. That being so such an arrangement cannot be described as a *quasi* partnership agreement to share in the profits of a venture. That contention of Mr. Sikri, therefore, again is untenable and must be repelled.

For the reasons given above I would answer questions 1 and 3 in the affirmative.

As regards questions 2 and 4 the matter to my mind is simple. These payments were part of the expenses incurred in canvassing custom

(1) (1931) 5 I. T. C. 363.

for sale of books published by the assessee. Selling books published by the assessee is a part of his trade. A customer has to be found willing to purchase his wares. Expenses incurred in finding a customer are in my view business expenses in the commercial sense of that term and must be deducted before net profits can be ascertained for tax purposes. The Tribunal held that this expenditure was incurred with an object in view, that is, to sell the books. In these circumstances it is difficult to see how this expenditure incurred for sale of books is expenditure incurred to secure business as found by the Tribunal.

Mr. Sikri argued that the expenditure was in the nature of illegal gratification given to the school authorities and being against public policy could not be allowed. But this position was never taken up before the Income-tax Officers or before the Tribunal and is outside the statement of the case contained in the reference and consequently cannot be entertained by us for the first time in this Court. Further, in my view there is no justification for this contention whatsoever. So far as I can see the expenditure is in the nature of a conventional commission paid by all persons carrying on the trade of printing and publishing to obtain custom. It is a part of the expense to earn profits. In my view, therefore, questions 2 and 4 should also be answered in the affirmative.

In view of the difficult problems involved in the case and taking into consideration all the material circumstances of this controversy I would make no order as to the costs of this reference.

DIN MOHAMMAD, J.—I agree that all the five questions raised by the Tribunal be decided in favour of the assessee. I also agree to the order of costs as proposed.

Reference answered accordingly.

[IN THE MADRAS HIGH COURT.]

YUVARAJAH OF PITHAPURAM AND ANOTHER

v.

COMMISSIONER OF INCOME-TAX, MADRAS.

SIR LIONEL LEACH, C. J., and PATANJALI SASTRI, J.

December 10, 1945.

INDIAN INCOME-TAX ACT (XI OF 1922), SEC. 2 (1)—INCOME FROM FORESTS AND FROM TREES GROWN WILD—WHETHER AGRICULTURAL INCOME—INCOME FROM PERMANENTLY SETTLED ESTATE—IMPOSITION OF INCOME-TAX—LEGALITY—WHETHER BREACH OF REGULATION XXV OF 1802.

The imposition of income-tax in respect of income other than agricultural income derived from a permanently settled estate would not be a breach of Regulation XXV of 1802 relating to permanent settlement.

CHIEF COMMISSIONER OF INCOME-TAX v. ZAMINDAR OF SINGAMPATTI [1922] (45 Mad. 518) *was impliedly overruled by the decision of the Privy Council in* PROBHAT CHANDRA BARUA v. KING EMPEROR [1930] (57 I. A. 228).

The income derived from forests of spontaneous growth by the sale of wood, bark, leaves, other usufruct of trees, minor forest produce and licence fees and from trees which have grown wild in non-forest areas is not agricultural income within the meaning of Section 2 (1) of the Indian Income-tax Act.

Cases referred to :—

Chief Commissioner of Income-tax v. Zamindar of Singampatti [1922] (I.L.R. 45 Mad. 518 ; 70 I.C. 504 ; A.I.R. 1922 Mad. 325 ; 1 I.T.C. 181).

Kaju Mal v. Salig Ram [1919-24] (A.I.R. 1919 Lah. 222 affirmed by P.C. in I.L.R. 5 Lah. 50).

Kesho Prasad Singh v. Sheo Pragash Ojha [1924] (46 All. 831 ; A.I.R. 1924 P. C. 247).

Probhat Chandra Barua v. King Emperor [1930] (57 I.A. 228 ; A.I.R. 1930 P.C. 209 ; 125 I.C. 871 ; 5 I.T.C. 1 ; I.L.R. 58 Cal. 430).

Province of Bihar v. Maharaja Pratap Udai Nath [1941] (9 I.T.R. 313 ; I.L.R. 20 Pat. 699 ; 194 I.C. 203 ; A.I.R. 1941 Pat. 289 ; 4 F.L.J. (H.C.) 109).

Sarojini Devi v. Subrahmanyam [1945] (I.L.R. 1945 Mad. 61).

Case referred to the High Court by the Income-tax Appellate Tribunal, Madras Branch, under Section 66 (1) of the Indian Income-tax Act, 1922 (Act XI of 1922), as amended by Section 92 of the Income-tax (Amendment) Act, 1939 (Act VII of 1939) in Application No. 66 R. A. No. 48 (Madras) of 1944-45 on its file for decision of the two questions of law mentioned in para. 4 of the Statement of Case: Case Referred No. 9 of 1945.

STATEMENT OF CASE.

" This application arises out of the Tribunal's order dated 30th June 1944 in R. A. A. No 222 (Madras) of 1943-44. The applicants have referred the following two questions of law for the opinion of the Honourable High Court at Madras :—

(1) Whether the permanently settled estate is liable for further taxation in the nature of income-tax?

(2) Whether forest income is not agricultural income exempt from taxation under the Indian Income-tax Act?

2. The facts of the case are that the applicants claimed exemption from tax in respect of a sum of Rs. 7,612 which they regarded as agricultural income. This sum is made up of the following items :—

Sale of bark, leaves and minor forest produce	...	Rs. 611
Sale of wood	...	" 6,346
Miscellaneous revenue sale of usufruct of trees	...	" 165
Tree owner's fees	...	" 57
Sale proceeds of trees in non-forest areas	...	" 433
		" 7,612

Two points were raised by the applicants, one with regard to the exemption of this sum from taxation on the ground that the income arose out of permanently settled estate which was exempt from further taxation and the other was that the income was agricultural income exempt from tax under Section 4 (3) (viii). The case of the applicants on both these points was very ably discussed by their advocate at the time of the hearing of the original appeal and a number of cases were cited. These are fully dealt with in the Tribunal's order under Section 33 (4) of the Act (Exhibit T. E.) The Tribunal ultimately decided the appeal against the appellants on both these points. The respondent, the Commissioner of Income-tax, Madras, in his written reply dated 29th December 1944, says that question No. 1 though no doubt a question of law has been finally settled by the decision of the Privy Council in *Rajah Probhat Chandra Barua* v. *Commissioner of Income-tax, Bengal*[1], which no doubt is a case relating to a permanent settlement under Bengal Regulation No. I of 1793. The Tribunal has applied that decision to the facts of this case, making no distinction between Bengal Regulation No. I of 1793 and Madras Permanent Settlement Regulation No. XXV of 1802. The respondent, however, is agreeable to refer the question in the following form :—

"Whether the imposition of income-tax in respect of income derived from the zamindari would be a breach of Regulation XXV of 1802 relating to permanent settlement?"

3. With regard to question No. 2 suggested by the applicants, the respondent desires that the following specific question may be referred in place of the very broad question put forward by the applicants :—

"Whether income derived from the sale of wood and minor products of wild forests of spontaneous growth will be exempt under Section 4, clause (3) (viii), read with Section 2, clause (1), of the Indian Income-tax Act of 1922?"

4. The details of the income under dispute are given hereinabove and it is stated by the Tribunal in its order that there were no special facts involved in the determination of that appeal. It was not urged by the applicants at the time of the hearing of the original appeal that for the purpose of earning the income recited above any agricultural operations had become essential. We would, therefore, refer the following two questions for the opinion of the Honourable High Court at Madras :—

(1) Whether the imposition of income-tax in respect of income derived from a permanently settled estate would be a breach of Regulation No. XXV of 1802 relating to permanent settlement?

(1) (1930) 58 Cal. 430; 5 I.T.C. 1.

(2) Whether the income of Rs. 7,612 derived from the sale of wood etc. (as detailed hereinabove), is exempt under Section 4 (3) (viii) read with Section 2 (1) of the Indian Income-tax Act of 1922?"

Ch. Raghava Rao, for the assessees.

C. S. Rama Rao Sahib, for the Commissioner.

JUDGMENT.

The assessees are the sons of the Maharajah of Pithapuram, the proprietor of the zamindari of Pithapur which was permanently settled under the Madras Permanent Settlement Regulation (Madras Regulation XXV of 1802). They are the joint proprietors of an estate settled upon them by their father. The estate which formed part of the zamindari of Pithapur includes certain forests from which the assessees derive income by the sale of wood, bark, leaves, other usufruct of trees, minor forest produce, and licence fees. They supplement this income by the sale of trees in non-forest areas of the estate held by them. It is admitted that the trees in the forest and non-forest areas have grown wild and that agricultural operations are not carried on in any of the areas. For the year of account 1941-42, the income from these sources amounted to Rs. 7,612 and the assessees were taxed on this sum for the year 1942-43. They maintained that they were exempt from taxation for two reasons. In the first place they said that the income was derived from the produce of a permanently settled estate which was free from all taxation, other than that imposed by way of *peishkush*, by reason of the provisions of the Madras Regulation. In the second place they contended that the income was agricultural income within the meaning of Section 2 (1) of the Indian Income-tax Act, 1922, and as such is exempt from income-tax by reason of Section 4 (3) (viii). The Income-tax Officer rejected both these pleas. His decision was upheld by the Appellate Assistant Commissioner and by the Income-tax Appellate Tribunal. At the request of the assessees, the Tribunal has, under Section 66 (1) of the Income-tax Act, referred for the opinion of this Court two questions. The Tribunal has worded them as follows:—

"(1) Whether the imposition of income-tax in respect of income derived from a permanently settled estate would be a breach of Regulation XXV of 1802 relating to permanent settlement.

(2) Whether the income of Rs. 7,612 derived from the sale of wood etc. (as detailed hereinabove), is exempt under Section 4 (3) (viii) read with Section 2 (1) of the Indian Income-tax Act, 1922."

The words "as detailed hereinabove" mean of course as detailed in the order of reference.

In *Chief Commissioner of Income-tax* v. *Zamindar of Singampatti* [1], a Special Bench of three Judges of this Court held that

(1) (1922) 45 Mad. 518.

income from a permanently settled estate was exempt from all taxation beyond the *peishkush* payable to Government. The precise question in that case was whether the income from forests and fisheries was agricultural income and therefore not chargeable to income-tax. The Court did not decide whether such income came within the definition of agricultural income, although it would appear that the learned Judges were inclined to the view that it was. They based their decision on the broad ground that the Madras Regulation and the sanad issued to the zamindar precluded further taxation by the Government. The sanad followed the provisions of the Regulation. In the present case, the sanad has not been produced, but it may be taken that it was also in accordance with the Regulation.

If the decision in *Chief Commissioner of Income-tax* v. *Zamindar of Singampatti* [1] stood alone we should be bound to answer the first question referred in favour of the assessees; but it does not stand alone. There is a judgment of the Privy Council of later date which has direct bearing. It was delivered in *Probhat Chandra Barua* v. *King Emperor*[2], where the same question arose with reference to the Bengal Permanent Settlement Regulation (Bengal Regulation I of 1793). Their Lordships pointed out that while that Regulation contains assurances against any claim to an increase of the *jama*, based on an increase of the zamindari income, no promise is given in it that a zamindar shall in respect of the income which he derives from his zamindari be exempt from liability to any future general scheme of property taxation, or that the income of the zamindari shall not be subjected with other incomes to any future general taxation of incomes.

The Bengal Regulation is differently worded from the Madras Regulation, but they are both to the same effect. Article 4 of the Bengal Regulation reads as follows :—

"The Governor-General in Council accordingly declares to the zamindars, independent talookdars and other actual proprietors of land with or on behalf of whom a settlement has been concluded under the Regulations abovementioned that at the expiration of the term of the settlement no alteration will be made in the assessment which they have respectively engaged to pay, but that they, and their heirs, and lawful successors, will be allowed to hold their estates at such assessment for ever."

The Madras Regulation opens with this statement :—

"Whereas it is known to the zamindars, mirasidars, raiyats and cultivators of land in the territories subject to the Government of Fort St. George that from the earliest until the present period of time the

(1) (1922) 45 Mad. 518. (2) (1930) 57 I. A. 228; 58 Cal. 430.

public assessment of the land revenue has never been fixed; but that, according to the practice of Asiatic Governments, the assessment of the land-revenue has fluctuated without any fixed principles for the determination of the amount, and without any security to the zamindars or other persons for the continuance of a moderate land-tax; that, on the contrary, frequent inquiries have been instituted by the ruling power, whether Hindu or Muhammadan, for the purpose of augmenting the assessment of the land revenue; that it has been customary to regulate such augmentations by the inquiries and opinions of the local officers appointed by the ruling power for the time being; and that in the attainment of an increased revenue on such foundations, it has been usual for the Government to deprive the zamindars, and to appoint persons on its own behalf to the management of the zamindaris, thereby reserving to the ruling power the implied right and the actual exercise of the proprietary possession of all lands whatever; and whereas it is obvious to the said zamindars, mirasidars, raiyats and cultivators of land that such a mode of administration must be injurious to the permanent prosperity of the country by obstructing the progress of agriculture, population and wealth, and destructive of the comfort of individual persons by diminishing the security of personal freedom and of private property; wherefore, the British Government, impressed with a deep sense of the injuries arising to the State and to its subjects from the operation of such principles, has resolved to remove from its administration so fruitful a source of uncertainty and disquietude, to grant to zamindars and other landholders, their heirs and successors, a permanent property in their land in all time to come, and to fix for ever a moderate assessment of public revenue on such lands, the amount of which shall never be liable to be increased under any circumstances."

In the clauses which follow effect is given to this declaration.

In *Probhat Chandra Barua* v. *King Emperor*[1], the Judicial Committee held that the zamindar of a permanently settled estate is assessable to Indian income-tax in respect of the income, profits and gains derived from his zamindari, subject to the exemptions provided in Section 4 (3) of the Act. The assessment should be computed after making proper allowance under Section 12 (2) in respect of the *jama* assessed and paid. Their Lordships affirmed the decision of the Calcutta High Court that the following items of the income derived by the appellant from his zamindari were not agricultural income and therefore not exempt from income-tax by Section 4 (3) (viii).

" (i) Jalkar or rents received from fisheries.

(ii) Ground rent from land used for potteries.

(iii) Ground rent from land used as brickfields.

(1) (1930) 57 I.A. 228; 58 Cal. 430.

(iv) Fees received from the tying-up of boats against the assessee's land.

(v) Fees received from land used for storing purchases of crops (*paliali*).

(vi) Fees received from cart-stands.

(vii) *Punyaha nazar* or *nazar* paid by tenants of agricultural holdings at the beginning of the zamindari year.

(viii) *Nazar* for petitions presented to the zamindar, dealing with questions of succession, settlement and partition of agricultural holdings.

(ix) Ground rent for permanent shops at *hauts* and *bazars*.

(x) Stall fees paid by temporary (daily) sellers at *hauts* and *bazars*."

The learned counsel for the assessees has not been able to advance any reason why this Court should not apply the decision in *Probhat Chandra Barua* v. *King Emperor*[1] to the Madras Regulation. If the Bengal Regulation permits of the profits and gains of a zamindari, other than those derived from agriculture, being assessed to income-tax, the same considerations must apply to the Madras Regulation. We hold that their Lordships' judgment impliedly overrules the judgment of this Court in *Chief Commissioner of Income-tax* v. *Zamindar of Singampatti*[2], and accordingly we answer the first question by saying that the imposition of income-tax in respect of income other than agricultural income derived from a permanently settled estate would not be a breach of the Madras Regulation.

We have now to decide whether the income derived from forests of spontaneous growth and from trees which have grown wild in non-forest areas represents agricultural income within the meaning of the definition given in Section 2 (1) of the Income-tax Act. As we have indicated, the learned Judges who decided *Chief Commissioner of Income-tax* v. *Zamindar of Singampatti*[2] were inclined to the view that income from forests and fisheries would be agricultural income, although they did not decide this question. It is very difficult to see how income from fisheries could be classified as agricultural income. In fact the decision of the Privy Council in *Probhat Chandra Barua* v. *King Emperor*[1] shows clearly that it cannot be so classified. Their Lordships did not, however, have to consider whether income from forests or individual trees of spontaneous growth comes within the definition and therefore it is necessary to examine the question for ourselves in the light of the reported cases which have bearing on it.

In *Province of Bihar* v. *Maharaja Pratap Udai Nath Sahi Deo*[3], the Patna High Court held that the income derived from wild jungle fruits was not income derived from land used for agriculture or

(1) (1930) 57 I.A. 228; 58 Cal. 430. (2) (1922) 45 Mad. 518. (3) (1941) 9 I.T.R. 313.

from agriculture and therefore was not assessable to income-tax under the Bihar Agricultural Income-tax Act, 1938.

In *Kaju Mal* v. *Salig Ram*[1], the Lahore High Court held that a stretch of natural forest which did not lie within a village site was exempt from pre-emption under the Punjab Pre-emption Act, 1905, as it was not agricultural land or land used for purposes subservient to agriculture, and this decision was upheld by the Judicial Committee in *Kaju Mal* v. *Salig Ram*[2]. Of course, what is agriculture within the meaning of the Indian Income-tax Act may not be agriculture within the meaning of another Act, as my learned brother pointed out when delivering the judgment of this Court in *Sarojini Devi* v. *Subrahmanyam*[3], but we think that the Lahore case does render material assistance in deciding the question now before us.

Another judgment of the Privy Council which has bearing is that delivered in *Kesho Prasad Singh* v. *Sheo Pragash Ojha*[4]. The question there was whether a mango grove was land used for agricultural purposes within the meaning of Section 79 of the Agra Tenancy Act, 1901, and it was held that it was not.

The Oxford Dictionary defines "agriculture" as "the science or art of cultivating the soil, including the allied pursuits of gathering in the crops and rearing live-stock; tillage, husbandry, farming (in the widest sense)." The word "agriculture" implies something which is achieved with the aid of human agency. In our judgment, income derived from trees which have grown wild cannot legitimately be described as agricultural income. In inclining to the opinion that income from forests was agricultural income, the learned Judges who decided *Chief Commissioner of Income-tax* v. *Zamindar of Singampatti*[5] were obviously influenced by the opinion which they had formed on the main question, namely, that no other tax beyond that involved in the payment of *peishkush* could be levied on income derived from a permanently settled estate. There is ample authority for holding that income derived from trees which have grown wild is not agricultural income, but without the aid of authority, we should have no hesitation in saying that to describe it as such would involve a distortion of the meaning of the word "agriculture."

We answer the second question referred by saying that the Rs. 7,612 does not represent agricultural income and is taxable.

As both the questions have been answered against the assessees, they must pay the costs of the reference which we fix at Rs. 250.

Reference answered accordingly.

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(1) A.I.R. 1919 Lah. 222.
(2) (1924) 5 Lah. 50.
(3) I.L.R. [1945] Mad. 61.
(4) (1924) 46 All. 831.
(5) (1922) 45 Mad. 518.

[IN THE PRIVY COUNCIL.]

COMMISSIONER OF INCOME-TAX, BENGAL

v.

GURUPADA DUTTA AND OTHERS.

LORD THANKERTON, LORD GODDARD and SIR JOHN BEAUMONT.

November 20, 1945.

INDIAN INCOME-TAX ACT (XI OF 1922), SEC. 10 (2) (ix), (xii) AND SEC. 10 (4)—PROFITS FROM BUSINESS—ALLOWANCES—RATE IMPOSED UNDER BENGAL VILLAGE SELF-GOVERNMENT ACT, 1919—WHETHER TAX ON PROFITS—WHETHER ALLOWABLE DEDUCTION.

The rate imposed under the provisions of the Bengal Village Self-Government Act, 1919, on a person occupying a building within the Union, and using the same for the purpose of business is an allowable deduction in computing the profits of the business under Section 10 of the Indian Income-tax Act.

The estimate of the annual income from business under the Bengal Village Self-Government Act can only proceed on a rough guess, which is in no way comparable with the ascertainment of profits and gains under the Income-tax Act and the inclusion of this element of business income as part of the 'circumstances' of the assessee with a view to the imposition of the union rate does not fall within Section 10 (4) of the Income-tax Act.

Where the union rate is not wholly referable to premises occupied for the purpose of a business or businesses, the assessee, on establishing the portion of the rate which is so referable, would be entitled to deduct such portion under Section 10 (2) (ix).

Appeal from a judgment of the Calcutta High Court dated 10th June 1943 and reported in [1943] (11 I.T.R. 499): P. C. Appeal No. 82 of 1944.

J. Millard Tucker, K.C., and *J. M. Pringle, K.C.*, for the appellant.

Respondents, *Ex parte.*

JUDGMENT.

LORD THANKERTON.—This is an appeal from the judgment of the High Court of Judicature at Fort William in Bengal, dated the 10th June, 1943, delivered on a reference made to it by the Appellate Tribunal under Section 66 of the Indian Income-tax Act, 1922. The respondents did not appear in the appeal.

The respondents constitute a Hindu undivided family carrying on business at Tejhati in Birbhum district, and also at Nalhati and

Lohapur, two other villages there. In assessing the respondents to income-tax for the year 1940-41, on the basis of the previous year 1939-40, the Income-tax Officer assessed the total assessable income of the respondents as a Hindu undivided family at Rs. 17,250, in which he included a sum of Rs. 6,563, as being the profits of the Nalhati business assessable under Sections 6 (iv) and 10 (1) of the Act. The Income-tax Officer disallowed a claim by the respondents to deduct as an allowance authorised by Section 10 (2) of the Act a sum of Rs. 84 paid by them as a union board rate in Nalhati under the provisions of the Bengal Village Self-Government Act, 1919. The respondents appealed under Section 30 against the order of the Income-tax Officer to the Appellate Assistant Commissioner of Income-tax, Calcutta, B Range, on various grounds, with only one of which the present appeal is concerned, namely, the claim to deduct the Rs. 84 above mentioned, but the Appellate Assistant Commissioner affirmed the disallowance of the deduction. The respondents then appealed under Section 33 of the Act to the Appellate Tribunal, who allowed the appeal, holding that the payment of the Rs. 84 was made for the purpose of the business and was an allowable deduction, in computing the profits of the Nalhati branch. On the application of the present appellant, the Tribunal made the reference under Section 66, the question referred being:

"Whether the rate imposed under the provisions of the Bengal Village Self-Government Act, 1919, on a person occupying a building within the union, and using the same for the purpose of business is an allowable deduction in computing the profits of the business under Section 10 of the Indian Income-tax Act?"

It will be convenient, in the first place, to state the relevant provisions of Section 10 of the Indian Income-tax Act, 1922, as it stood amended at the material date:

"10. (1) The tax shall be payable by an assessee under the head 'profits and gains of business, profession or vocation' in respect of the profits or gains of any business, profession or vocation carried on by him.

(2) Such profits or gains shall be computed after making the following allowances, namely:—

* * * *

(ix) any sums paid on account of land revenue, local rates or municipal taxes in respect of such part of the premises as is used for the purposes of the business, profession or vocation;

* * * *

(xii) any expenditure (not being in the nature of capital expenditure or personal expenses of the assessee) laid out or expended

wholly and exclusively for the purpose of such business, profession or vocation;

* * * *

(4) Nothing in clause (ix) or clause (xii) of sub-section (2) shall be deemed to authorise the allowance of any sum paid on account of any cess, rate or tax levied on the profits or gains of any business, profession or vocation or assessed at a proportion of or otherwise on the basis of any such profits or gains........."

In answering affirmatively the question of law submitted to them the learned Judges contented themselves with expressing agreement with the opinion of the Appellate Tribunal and their reasons therefor.

The main argument for the Crown was based on sub-section (4) of Section 10 of the Income-tax Act. It was admitted that the union board rate was a local rate and that it was not levied on the profits or gains of the Nalhati business, but it was maintained that the union board rate was assessed at a proportion of or otherwise on the basis of the profits or gains of the Nalhati business.

Alternatively, it was maintained by the Crown that the respondents had failed to bring the rate here in question within either head (ix) or head (xii) of sub-section (2) of Section 10 for reasons to which their Lordships will refer later.

The Bengal Village Self-Government Act, 1919 (Bengal Act V of 1919), was intended to develop self-government in the rural areas of Bengal, and the financial provisions are contained in Chapter V of the Act. The material sections of the Act and the material rules made under Section 101 (2) (k) of the Act are as follows:—

"Section 37. The union board shall impose yearly on persons who are owners or occupiers or owners and occupiers of buildings, within the union, a rate amounting to—

(a) the sum required, after deduction of the contribution, if any, made by the Provincial Government in this behalf, for the salaries and equipment of the defadars and chaukidars and the salaries of the establishment of the union board, and

(b) the sum estimated to be required to meet the expenses of the board in carrying out any of the other purposes of this Act, if such estimate has been approved by more than half the total number of the members of the board at a meeting specially convened for the purpose, together with ten per cent. above such sums to meet the expenses of collections and the losses due to non-realisation of the rate from defaulters.

Section 38. (1) The rate to be imposed by a union board under Section 37 shall be an assessment according to the circumstances

within the union and property within the union, if any, of the persons liable to the same:

Provided that the amount assessed upon any person in any one year shall not be more than eighty-four rupees.

(2) Any person who, in the opinion of the union board, is too poor to pay half an anna a month, shall be altogether exempted from payment of any rate under this Act.

Section 39. The assessment for the imposition of the rate under Section 37 shall be made in accordance with rules prescribed under Section 101, and any person dissatisfied with the amount at which he has been assessed may, within such time as may be specified in those rules, apply to the union board, either orally or in writing, for a revision of the assessment, and the union board may amend the assessment or confirm the same.

* * * *

Section 101. (1) The Provincial Government may, after previous publication, make rules to carry out the purposes of this Act.

(2) In particular and without prejudice to the generality of the foregoing power the Provincial Government may make rules......

(k) for the making of an assessment by the union board under Section 39, for imposing the rate under Section 37, and prescribing under Section 41 the method and time of payment of such rate.

RULES MADE UNDER SECTION 101 (2) (k) THEREOF.

ASSESSMENT AND IMPOSITION OF THE UNION RATE.

RULE 1. (1) After preparing the annual budget estimate in Account Form No. 1 and not less than two months and a half before the first day of the year to which the budget relates, the union board at a meeting shall proceed to assess the union rate provided in the estimate according to the circumstances and the property within the union of the person liable to assessment:

Provided that the said period may, for reasons to be recorded in writing, be at any time altered by the District Magistrate.

(2) When a union board is for the first time constituted in any union it may assess the union rate for a portion of the year in which it is so constituted or of the year next following.

RULE 2. The union board shall first prepare, village by village and in Form No. 1, a list of all persons owning or occupying buildings, whether with or without land appertaining thereto, in the union, either permanently or temporarily, showing their trade, business, etc., within the union, and the estimated annual income which they derive from buildings or other property or business within the union. All such persons shall be included in the list even if some are subsequently exempted,

RULE 3. The board shall, after considering his debts and liabilities, if any, determine the total assessable income of the person concerned, *i.e.*, the income which he derives from business conducted, or from buildings or other property held, within the union.

* * * *

RULE 5. No person shall be assessed who does not own or occupy a building within the union. A person who, though liable to pay the rate, does not reside within the union, shall be assessed on the buildings which he owns or occupies within the union, and on any income which he derives from business conducted, or from landed or other property held, within the union.

Explanation.—Ownership or occupation includes part ownership or occupation, and ownership or occupation of a building or part of a building for any portion of the year shall render the owner or occupier liable to pay the rate.

Note.—A person should be deemed to be in occupation of a building who pays the rent of the building directly or indirectly.

* * * *

RULE 10. The assessment list, after being checked by the Circle Officer, or the revised list, if any, prepared under rule 9, shall be published by the union board in the manner laid down in rule 6, if possible before the first day of the year, and if not, as soon as possible thereafter.

RULE 11. If any person mentioned in the assessment list ceases at any time after the publication thereof under rule 10 to occupy any building in respect of the occupation of which he has been assessed, or if the means and property in respect of which he has been so assessed are reduced, the union board at a meeting may exempt him from assessment or revise the same; and such exemption or revision shall take effect from such date as the board may direct."

It is clear that the rate is only imposed on persons who are owners or occupiers or owners and occupiers of buildings within the union, but, in arriving at the amount to be assessed on any such person, it is provided by Section 38 (1) that the assessment is to be according "to the circumstances within the union and property within the union, if any," of the assessee, with a maximum limit of Rs. 84 in any one year in the case of any assessee. Under Section 39 the assessment for the imposition of the rate is to be made in accordance with rules prescribed under Section 101.

In order to determine under rule 3, "the total assessable income of the person concerned, *i.e.*, the income which he derives from business conducted, or from buildings or other property held, within the union," the board have before them the information prepared under rule 2,

which shows the buildings occupied or owned in the union, permanently or temporarily, and also "their trade, business, etc., within the union, and the estimated annual income which they derive from buildings or other property or business within the union."

It will be noted that, in the absence of the necessary powers and machinery, which are not provided by the Act, the estimate of the annual income from business can only proceed on a rough guess, which is in no way comparable with the ascertainment of profits and gains under the Income-tax Act, and, in the opinion of their Lordships, the inclusion of this element of business income as part of the "circumstances" of the assessee with a view to the imposition of the union rate does not fall within sub-section (4) of Section 10 of the Income-tax Act. It is conceded that the union rate is not "levied on the profits or gains," which clearly implies an ascertainment of such profits and gains, and the words "assessed . . . . on the basis of any such profits or gains" in the later part of the sub-section must also be so limited. No such ascertainment of the profits and gains of the business can be undertaken for the purposes of the union rate. The main argument for the Crown therefore fails.

Turning now to head (ix) of sub-section (2) of Section 10 of the Income-tax Act, the argument for the Crown proceeded on a somewhat meticulous examination of the statement of the case, and the papers in the index which are made part of the reference, in order to show that the respondents, in addition to the premises in which they carry on the Nalhati business, have house property in the village, which would show that the rate was only partly related to the premises used for the purposes of the business, and that the respondents have failed to establish what part of the Rs. 84 is so referable. In the opinion of their Lordships, the decision of the Appellate Tribunal, the question of law referred, and the decision of the High Court, proceed on the footing that the Rs. 84 solely relates to the premises occupied for the purpose of the Nalhati business, and, it being admitted that the union rate is a local rate, the question falls to be answered in the affirmative. Their Lordships may add, however, that in any case where the union rate is not wholly referable to premises occupied for the purpose of a business or businesses, the assessee, on establishing the portion of the rate which is so referable, would be entitled to deduct such portion under head (ix). In this view, no separable question appears to arise under head (xii), and, in any event, it would be unnecessary to deal with it.

Their Lordships will, therefore, humbly advise His Majesty that the appeal should be dismissed, and that the judgment of the High Court should be affirmed. *Appeal dismissed.*

[IN THE PATNA HIGH COURT.]

COMMISSIONER OF INCOME-TAX, BIHAR AND ORISSA

v.

S. K. SAHANA & SONS.

FAZL ALI, C. J., and MANOHAR LALL, J.

December 12, 1945.

INDIAN INCOME-TAX ACT (XI OF 1922), SEC. 10 (2) (vi)—DEPRECIATION ALLOWANCE—TRANSFER OF BUSINESS IN ACCOUNTING YEAR—WHETHER TRANSFEROR ENTITLED TO FULL DEPRECIATION ON MACHINERY AND BUILDING.

The assessee carrying on a business in mica and rice mill transferred the business along with the machinery and building to a joint stock company on 1st January 1940. The assessee was keeping its accounts from April to April. In the assessment for the year 1940-41 the Income-tax authorities held that as the assessee had ceased to be the owner of the mill and building on 1st January 1940, it could not claim depreciation allowance under Section 10 (2) (vi) of the Income-tax Act for the entire period of twelve months, but could only claim proportionate depreciation for 8½ months :

Held, *that the Income-tax Act did not authorise the apportionment of depreciation allowance in such a case as this and the assessee was therefore entitled to the full amount of depreciation under Section 10 (2) (vi).*

Commissioner of Income-tax, Bihar and Orissa v. *Dalmia Cement Co., Ltd.* [1945] (13 I.T.R. 415), *referred to.*

Reference under Section 66 (1) of the Indian Income-tax Act (XI of 1922) by the Income-tax Appellate Tribunal, Bombay: Miscellaneous Judicial Case No. 88 of 1945.

STATEMENT OF CASE.

"This is an application under Section 66 (1) of the Indian Income-tax Act, made by the Commissioner of Income-tax, Bihar and Orissa, for the purpose of referring the following question of law for their Lordships' opinion :—

"Is the assessee entitled to the full amount of depreciation under Section 10 (2) (vi) of the Income-tax Act irrespective of the period of user ?"

2. The respondent in this case, Messrs. S. K. Sahana & Sons, is represented by Mr. S. K. Sawday, Income-tax practitioner. No written reply has been sent by the respondent as to whether he objected to the

question being referred to the Honourable High Court, but Mr. Sawday, who appeared before us admitted that the question as framed by the Commissioner of Income-tax is a question of law and should be referred to the Honourable High Court. The facts of this case are simple.

3. **Statement of the Case.**—The respondent is a Hindu undivided family. For the years prior to the relevant accounting year the Bengali year was adopted by it for the purpose of keeping its accounts. This Bengali year runs from the middle of April in one year to the middle of April in the following year. The Hindu undivided family had business in mica and rice mill. On 1st January 1940, the respondent transferred its business to a joint stock company. The accounts of the Hindu undivided family were, therefore, made up for the relevant accounting period from 14th April 1939 to 31st December 1939—about 8½ months.

4. The respondent claimed depreciation for machinery, building, etc., under Section 10 (2) (vi), for the whole period of 12 months instead of 8½ months for which the respondent was the owner and after which period the business was transferred to the limited company. The department refused to allow 12 months' depreciation as claimed by the respondent but allowed only 8½ months' depreciation. The Appellate Tribunal held that the apportionment of depreciation allowance in regard to time was not warranted by the section when the asset was wholly used for the purposes of the business, the allowance prescribed was for each assessment whatever may be the period of the previous year. The full amount of depreciation for 12 months, as claimed by the respondent, was therefore, allowed. The Commissioner has asked us to refer the above question of law, arising out of the order of the Tribunal, to the Honourable High Court.

5. We think that a question of law does arise from the Tribunal's order and the question, as mentioned above, is, therefore, referred to their Lordships for their opinion."

S. N. Dutt, for the Commissioner.

R. S. Chatterjee, for the assessee.

JUDGMENT.

MANOHAR LALL, J.—This is a reference at the instance of the Commissioner of Income-tax, Bihar and Orissa, by the Appellate Income-tax Tribunal asking for the opinion of the Court on the question: "Is the assessee entitled to the full amount of depreciation under Section 10 (2) (vi) of the Income-tax Act irrespective of the period of user?"

The facts are not in dispute. The assessee is a Hindu undivided family and had a business in mica and rice mill. The assessee keeps his account according to the Bengali year from April to April. In the assessment for the year 1940-41, the assessee claimed depreciation for machinery and building for the entire period of twelve months instead of eight and a half months even though on the first January, 1940, the assessee had transferred all his business in mica and rice mill along with the machinery and building to a joint stock company. The department allowed depreciation only for $8\frac{1}{2}$ months upon their view that the assessee ceased to be the owner of the mill and building on the 1st of January, 1940, and, therefore, could not claim depreciation for the entire twelve months. The Appellate Tribunal however, held that the Indian Income-tax Act did not authorise any apportionment of the depreciation allowance in regard to time. Hence the reference at the instance of the Commissioner.

The relevant provisions of the Act are contained in Section 10 (2) (vi) which entitles the assessee to claim depreciation of the buildings, machinery, plant or furniture used by him for the purpose of business, profession or vocation. It is not disputed that the assessee was the owner of the building, machinery etc., during the accounting year. I do not see any provision in the Act which authorises an apportionment of depreciation on the assessee having sold the machinery or plant during the accounting period. The legislature was aware that a machinery or plant might be sold or discarded during the accounting year and in such events it is provided by Section 10 (2) (vii) that the amount by which the written down value of the machinery or plant exceeds the amount for which the machinery or plant is actually sold or its scrap value is a deductible allowance and also that where the amount for which the machinery or plant is sold exceeds the written down value, the excess is to be deemed to be the profits of the previous year in which the sale took place.

Learned Advocate for the assessee also drew attention to Section 10 (3) which provides that where a building or machinery for which allowance is due is not wholly used for the purpose of business, profession or vocation, the allowance is restricted to a fair proportional part of the amount which would be allowable if such building or machinery was wholly so used. He argues, that the legislature has directed an apportionment only in such a case and that there is no justification for extending the rule of apportionment to other cases. The contention, in my opinion, is sound. Our attention was drawn to a recent case decided by this Bench on the 15th August, 1945—*Commissioner of Income-tax, Bihar and Orissa* v. *Dalmia Cement Co. Ltd.*[1]

(1) (1945) 13 I.T.R. 415.

In that case my Lord the Chief Justice, who delivered the judgment of the Bench, negatived the contention raised on behalf of the Income-tax department as to the meaning sought to be given to Section 10 (3) and observed: "The words 'not wholly used for the purposes of the business, profession' etc., do not mean not used throughout the year or during the whole of the year in question. They mean that the building, machinery etc., have not been used exclusively for the purpose of the profession or vocation, that is to say, they have been used for other purposes also. There is no such provision in the Act as would justify the view that if the machinery is not used throughout the year, then the period for which it has worked should be calculated and depreciation should be allowed in proportion to such period." The argument advanced on this occasion before us on behalf of the department is similar. I am of opinion that there is no such provision in the Act as would justify the view that if the machinery is not the property of the assessee throughout the year then the period for which it was the property of the assessee should be calculated and depreciation should be allowed in proportion to such period. It is not denied that the assessee as the owner of the machinery and building was using it during the accounting period for the purpose of business and he is being assessed on the profits which he made for the period during which he was the owner. It was contended by the learned standing counsel that the acceptance of this view is most inequitable as it would enable both the transferor and the transferee to claim full deduction for the depreciation although the machinery etc., have been used by either of them only for a broken period in the same year. But it has been rightly pointed out that equity and taxation are as poles asunder and the Court cannot invoke an equitable rule in the construction of a taxing statute.

For these reasons, in my view, the Appellate Tribunal has come to a correct conclusion, and I would answer the question in the affirmative.

The assessee is entitled to the costs of this Court; hearing fee Rs. 250.

FAZL ALI, C. J.—I agree.

Reference answered in the affirmative.

[IN THE MADRAS HIGH COURT.]

COMMISSIONER OF INCOME-TAX, MADRAS
v.
SRI VISWESWARDAS GOKULDAS.

SIR LIONEL LEACH, C. J., and PATANJALI SASTRI, J.

December 14, 1945.

INDIAN INCOME-TAX ACT (XI of 1922), SEC. 13—METHOD OF ACCOUNTING—VALUATION OF STOCK—VALUATION AT COST PRICE BOTH AT BEGINNING AND END OF YEAR—CHANGE OF METHOD—PERMISSIBILITY—REVISION OF VALUATION BY INCOME-TAX OFFICER—LEGALITY.

The assessee, a merchant, adopted as the method of accounting for income-tax purposes the practice of valuing his stocks at the cost price both at the beginning and at the end of the year. In the Samvat year 1995 the assessee opened the account with stocks valued at cost price and closed it with a valuation at the market price which was much higher than the cost price. The Income-tax Officer accepted the assessee's return for the Samvat year 1995 which corresponded to the year of assessment 1940-41. In the following year the Income-tax Officer discovered that he had made a mistake in accepting the method of accounting adopted by the assessee for the year 1940-41 and assessed the assessee for the Samvat year 1996 (1941-42) on the basis of the cost price of the stock both at the beginning and at the end of the year which resulted in the addition of Rs. 24,855 to the total income :

Held, *that in the circumstances of the case the assessment made by the Income-tax Officer for 1941-42 by adding the sum of Rs. 24,855 to the total income of the assessee by revising valuations of the opening and closing stocks of Samvat year 1996 on cost basis was legal.*

The proviso to Section 13 gives the Income-tax Officer full liberty of action if he is satisfied that the method adopted by the assessee does not allow of a correct assessment of the profits. When he is of this opinion it is his bounden duty to adopt another method, a method which he considers will permit of a satisfactory assessment.

Cases referred to:—

Commissioner of Income-tax, Bombay *v.* Sarangpur Cotton Manufacturing Co., Ltd. of Ahmedabad [1938] (6 I.T.R. 36; 65 I.A. 1; I.L.R. 1938 Bom. 239; 172 I.C. 1; 47 L.W. 9; 40 Bom. L.R. 227; A.I.R. 1938 P.C. 1; 1938, 1 M.L.J. 1).

Commissioner of Income-tax, Madras *v.* Chengalvaraya Chetti [1925] (48 Mad. 836; 2 I.T.C. 14).

Case referred to the High Court by the Income-tax Appellate Tribunal, Bombay, under Section 66 (1) of the Indian Income-tax Act, 1922 (Act XI of 1922), as amended by Section 92 of the Income-tax

(Amendment) Act, 1939 (Act VII of 1939), in 66 R.A. No. 29 (Madras) of 1944-45 on its file for the decision of the question of law mentioned in para. 5 of the Statement of Case: Case Referred No. 7 of 1945.

STATEMENT OF CASE.

" This reference application, which is made by the Commissioner of Income-tax, Madras, arises out of our order dated 9th June 1944 in R. A. A. No. 6. (Madras) of 1943-44.. The facts of the case may be briefly stated as under :—

The original appeal before us was with regard to the assessment year 1941-42 which had for its previous year the Samvat year 1996 (12th November 1939 to 30th October 1940). That appeal arose as a result of the Income-tax Officer revising the values of the opening as well as closing stocks of Samvat year 1996 and adopting figures other than those adopted by the respondent. Up to and including Samvat year 1994, the respondent was valuing his stocks at cost price. Therefore, for the Samvat year 1995 the opening stock was also valued at cost price. At the end of Samvat year 1995 the respondent, for the first time, valued the stock at market price which was found to be higher than the cost price. The valuation was accepted by the Income-tax Officer and assessment for the tax year 1940-41 was made by him on the basis of this valuation. While making assessment for 1941-42, the Income-tax Officer objected to the change in the basis of valuation and he valued both the opening as well as the closing stocks for Samvat year 1996 at cost price, thus adding a net sum of Rs. 24,855 to the profit of the respondent and also stated that he would revise the assessment for 1940-41 under Section 35 of the Act, adopting the correct value for stocks at the end of Samvat year 1995.

2. For the purpose of ascertaining the correct working results of a business for any year, the normal basis of valuation to be followed in case of stock-in-trade is cost price or market price whichever is the lower on the date of the balance sheet. As stated above, the respondent was valuing his stocks at cost price up to and including Samvat year 1994. At the end of Samvat year 1995 he altered the basis of valuation to market price and the market price at that time was really above the cost price. Though the valuation was not according to the principle enunciated above, *viz.*, cost price or market price whichever is less, the same was accepted by the Income-tax Officer for the purpose of that assessment, and as a result of this the respondent paid an excess tax of Rs. 9,126-8-0. The market value basis having been accepted by the department while making assessment on the profits of Samvat year 1995, the same value had necessarily to be adopted as the value of opening stock for Samvat year

1996. This, the respondent stated, was in accordance with the ruling in *Commissioner of Income-tax, Madras* v. *Chengalvaraya Chetti and Munisamy Chetti*[1]. The point decided in that case was that an assessee having once adopted a particular value for his closing stock of one year cannot change it when it becomes the opening stock of the next year for the next year's assessment. The opening stock for Samvat year 1996 having been valued at market price, the respondent valued the closing stock also at market price. This, it was stated on behalf of the respondent, was in accordance with the ruling in *Commissioner of Income-tax, Bombay* v. *Ahmedabad New Cotton Mills Co., Ltd.*[2] The point decided in that case was that the opening and the closing stocks of any account year must both be valued on the same basis. The departmental representative argues that the decision in *Commissioner of Income-tax, Madras* v. *Chengalvaraya Chetti and Munisamy Chetti*[1] is to be followed only in a case where the valuation is made on correct basis and not when it is definitely found that the valuation is incorrect. The Tribunal, however, decided the case *following the rulings in both the above-mentioned cases* but without making the distinction which the departmental representative was trying to make with regard to correct and incorrect bases of valuation. The Tribunal in arriving at its finding was more guided by the fact that the Income-tax Officer while making assessment for 1940-41 had accepted the altered basis of valuation followed at the end of Samvat year 1995 and that in accepting the same, the department had signified its assent to the change in the basis of valuation, more particularly because the change resulted in collection of a larger amount of tax than would have been otherwise paid by the respondent. Besides, the revision contemplated by the Income-tax Officer in the assessment for 1940-41 under Section 35 of the Act was not made even up to the time of the hearing of the appeal by the Tribunal in June 1944. As the rectification proposed to be made by the Income-tax Officer was actually resulting in reduction of the tax, there was no reason for the delay in making the revision. The departmental representative stated that the respondent was not co-operating with the department in the matter of this revision, and had not replied to the notice given to him under Section 35 of the Act. From a reading of Section 35 of the Act, we find that such a notice is essential only where the proposed rectification results in an enhancement of an assessment, but as in this case the rectification was not going to result in an enhancement of the assessment, no notice need have been sent to the respondent and the department need not have waited for any co-operation on the part of the respondent. We do not think

(1) (1925) 48 Mad. 836. (2) (1930) 4 I.T.C. 245.

that the reason given by the departmental representative is substantial. The applicant now desires us to append as exhibits copies of the Income-tax Officer's letters to the respondent, dated 7th January 1942 and 9th February 1942, but as these letters were neither placed before us nor referred to us at the time of the hearing of the original appeal we cannot allow these to form part of the reference. Moreover, we have held above that in the circumstances of this case, no notice or letters need have been sent by the Income-tax Officer to the respondent for action under Section 35 of the Act. These letters, therefore, need not be printed.

3. The Commissioner in paragraph 4 (a) of his application states that the Bench overlooked the fact that it is the accepted rule to value the stock either at cost price or at market price whichever is less. In reply to this statement, it is to be mentioned that this fact was not overlooked by the Tribunal but the Tribunal was prevented, in view of the decisions in *Commissioner of Income-tax, Madras* v. *Chengalvaraya Chetti* [1] and *Commissioner of Income-tax, Bombay* v. *Ahmedabad New Cotton Mills Co., Ltd.* [2], already referred to hereinabove, from arriving at any decision other than that to which it ultimately came. The Tribunal does not think that, as claimed in paragraph 4 (b) of the application, the deviation in the basis of valuation from cost price to market price, made in Samvat year 1995, escaped the notice of the Income-tax Officer, inasmuch as the Income-tax Officers are particular in making enquiries about the basis of valuation of the stock in cases of assessments of all traders. The Tribunal is also not satisfied that the Income-tax Officer, while making the assessment for 1940-41, omitted to verify the valuation of the closing stock and the consequent deviation from the method adopted in previous years. There is nothing on record which would show this omission on his part. In paragraph 4 (d) of his application, the Commissioner makes reference to a letter dated 13th August 1941, from the respondent to the Income-tax Officer. It is necessary to state that no such letter was either placed before the Tribunal or referred to at the time of hearing by either of the parties at dispute, and the Tribunal is not bound to take into consideration any correspondence or evidence that was not referred to or placed before it at the time of the hearing of the appeal. In paragraph 4 (e) of the application, the Commissioner makes reference to the steps taken by the Income-tax Officer towards revising the assessment for 1940-41 and to the default on the part of the respondent. We have already mentioned earlier that it was not necessary for the department to address any communication to the respondent for the purpose of revising the assessment under Section 35 of the Act and

(1) (1925) 48 Mad. 836. (2) (1930) 4 I.T.C. 245.

that the Income-tax Officer could have easily completed the revision without waiting for any response on the part of the respondent. In paragraph 4 (f) of the application, the Commissioner refers to the saving made by the respondent of a sum of about Rs. 15,500 in the tax payable by him in respect of his profits for Samvat year 1996. As noted by us earlier, the respondent has already paid an excess tax of Rs. 9,126-8-0 in respect of assessment of his income for Samvat year 1995. The Tribunal's decision, as mentioned earlier, was based on the rulings in the two cases mentioned above, as also on the facts of this case. The Commissioner has asked us to refer the following question of law to the Honourable High Court at Madras :—

"Whether the Income-tax Officer was not entitled and bound in law in the circumstances of this case to revise the valuation of the opening and closing stocks of Samvat year 1996 (assessment year 1941-42) according to cost price which was less than market price, which was the method of valuation adopted by the respondent in prior years and to make consequential adjustments in the assessment for 1940-41 (Samvat year 1995)."

4. Having already laid out the circumstances of this case in brief, we consider that the proper question which can be referred to the Honourable High Court will be the one suggested by the respondent in his reply dated 5th December 1944. The question is as follows and we refer it to the Honourable High Court at Madras under Section 66 (1) of the Income-tax Act :—

Question referred.—"Whether in the circumstances of the case, the assessment made by the Income-tax Officer for 1941-42 by adding the sum of Rs. 24,855 to the total income of the respondent by revising valuations of the opening and closing stocks of Samvat year 1996 on cost basis was legal."

C. S. Rama Rao Sahib, for the Commissioner.
P. R. Srinivasan, for the assessee.

JUDGMENT.

(Judgment of the Court was delivered by the Honourable the Chief Justice.)

The assessee is a merchant dealing in metals. Up to the end of the Samvat year 1994, that is up to 23rd October 1938, he adopted as the method of accounting for income-tax purposes the practice of valuing his stocks at the cost price. Both at the beginning and at the end of the year the cost price was taken. In respect of the Samvat year 1995 (20th October 1938 to 11th November 1939) the assessee made a change. He opened the account with stocks valued at cost price and

closed it with a valuation at the market price. The market price was much higher than the cost price and this resulted in showing an increase in the profits to the extent of Rs. 24,797. The object of the change in the method of accounting is not far to seek. The Excess Profits Tax Act had come into operation. It actually came into force on the 13th April 1940, but the Legislature applied its provisions from the 1st September 1939. The Income-tax Officer accepted the assessee's return for the Samvat year 1995 which corresponded to the year of assessment 1940-41. In the following year the Income-tax Officer discovered that he had made a mistake in accepting the method of accounting which the assessee had adopted for the year 1940-41. Consequently for the Samvat year 1996 (1941-42) the Income-tax Officer assessed the assessee on the basis of the cost price of the stock. He took the cost price at the beginning of the year and at the end of it, which meant the addition of Rs. 24,855 to the total income. The assessee objected and said that the Income-tax Officer should have adopted the method which had been adopted for the previous year. He appealed to the Assistant Commissioner of Income-tax without success, but on a further appeal to the Income-tax Appellate Tribunal, Madras Bench, he was successful. At the request of the Commissioner of Income-tax the Tribunal has referred to this Court under Section 66 (1) of the Income-tax Act the following question :—

"Whether in the circumstances of the case the assessment made by the Income-tax Officer for 1941-42 by adding the sum of Rs. 24,855 to the total income of the respondent by revising valuations of the open ing and closing stocks of Samvat year 1996 on cost basis was legal."

Section 13 of the Income-tax Act, 1922, deals with the method of accounting. It says that income, profits and gains shall be computed for the purposes of Sections 10 and 12 in accordance with the method of accounting regularly employed by the assessee provided that, if no method of accounting has been regularly employed, or if the method employed is such that, in the opinion of the Income-tax Officer, the income, profits and gains cannot properly be deduced from it, then the computation shall be made upon such basis and in such manner as the Income-tax Officer may determine. The proviso gives the Income-tax Officer full liberty of action if he is satisfied that the method adopted by the assessee does not allow of a correct assessment of the profits. When he is of this opinion it is his bounden duty to adopt another method, a method which he considers will permit of a satisfactory assessment. This was pointed out by the Privy Council in *Commissioner of Income-tax, Bombay* v. *Sarangpur Cotton Manufacturing Co., Ltd., of Ahmedabad*[1].

(1) (1938) 6 I.T.R. 36; I.L.R. [1938] Bom. 239.

In *Commissioner of Income-tax, Madras* v. *Chengalvaraya Chetti*[1], this Court held that it was an accepted rule that the assessee in crediting the closing stock figure is to take either the cost price or the market price whichever be the less—a provision obviously intended to be in favour of the trader and one which enables him more evenly to distribute his loss.

Taking the stock for the Samvat year 1995-1996 at the market price was not in accordance with the assessee's regular method of accounting. His regular method had been to take the cost price both at the beginning and at the end of the year. Moreover the market price was admittedly far higher than the cost price. In these circumstances the Income-tax Officer took the proper course in valuing the stocks at the cost price, at the same time offering to rectify the assessment for the previous year under the provisions of Section 35 of the Act. We hold that the Income-tax Officer was in law entitled to adopt the course which he did in respect of the Samvat year 1996 and accordingly we answer the question referred in the affirmative.

The learned counsel for the Commissioner of Income-tax has given an undertaking to the Court that the assessment for the year 1940-41 will be revised. In respect of that year also the stocks will be valued at the opening and at the close of the year at the cost price and the tax repayable to the assessee on this basis will be adjusted.

The Commissioner of Income-tax is entitled to the costs of this reference, which we fix at Rs. 250.

Reference answered in the affirmative.

[IN THE BOMBAY HIGH COURT.]

WAMAN SATWAPPA KALGHATGI

v.

COMMISSIONER OF INCOME-TAX.

KANIA, AG. C. J., and CHAGLA, J.

September 18, 1945.

INDIAN INCOME-TAX ACT (XI OF 1922), SEC. 25A—HINDU UNDIVIDED FAMILY—PARTITION—PARTITION OF BUSINESSES AND MOVABLES WITHOUT PARTITION OF IMMOVABLE PROPERTIES—BUSINESSES SEPARATELY CARRIED ON BY MEMBERS—INCOME FROM BUSINESS—WHETHER SEPARATE INCOME OF MEMBERS OR INCOME OF FAMILY—SCOPE OF SEC. 25A.

The assessee, a Hindu undivided family, was possessed of lands and buildings as well as cash and jewellery and was carrying on

(1) (1925) 48 Mad. 836.

several businesses. In July 1941, the members decided to separate and started making a division of the family cash, jewellery and businesses and completed it on July 30, 1941. The division was embodied in a memorandum which they executed that day. The members thereafter separately carried on those businesses which were assigned to their respective shares. The shares of the members in the movables and businesses did not correspond exactly with the interest which they possessed in the family estate according to Hindu law and there was disagreement amongst them as regards the division of the immovable properties. Therefore on July 31, 1941, the parties submitted a reference to arbitration for division and final adjustment of shares, and the award was made on October 16, 1941. The assessee's previous year was the Hindu year commencing from October 31, 1940, and ending on October 20, 1941. In the assessment year 1942-43, the question arose whether the income of the businesses between July 30, 1941, and October 20, 1941, should be included in the total income of the Hindu undivided family.

Held, *that there was nothing in law to prevent the members of a joint family which had become disrupted from parting with individual assets either to a stranger or to one of themselves and that as the businesses in the present case were individually allotted and worked by the members separately for their own benefit, the profits and gains of the businesses for the period from July 30, 1941, to October 20, 1941, were the individual income of the members and could not be included in the total income of the family.*

Sir Sundar Singh Majithia v. *Commissioner of Income-tax* [1942] (10 I.T.R. 457) and *Bansidhar Dhandhania* v. *Commissioner of Income-tax* [1944] (12 I.T.R. 126) relied on.

Cases referred to:—

Bansidhar Dhandhania *v.* Commissioner of Income-tax [1944] (12 I.T.R. 126; I.L.R. 23 Pat. 68; A.I.R. 1944 Pat. 137).

Medam Gurumurthy Setty *v.* Commissioner of Income-tax [1944] (12 I.T.R. 176).

Sir Sundar Singh Majithia *v.* Commissioner of Income-tax [1942] (10 I.T.R. 457; 202 I.C. 483; A.I.R. 1942 P.C. 57; I.L.R. 1943 All. 69; 45 Bom. L.R. 9).

Reference under Section 66 (1) of the Indian Income-tax Act by the Income-tax Appellate Tribunal: Income-tax Reference No. 2 of 1945.

STATEMENT OF CASE.

" This is a reference under Section 66 (1) of the Indian Income-tax Act as amended in 1939, upon an application of the applicant Mr. Waman Satwappa Kalghatgi. The Commissioner of Income-tax, Bombay, Sind and Baluchistan, has filed a written answer. The two are, respectively, Exhibits A and B in the appended list.

2. The applicant invites us to submit two questions for their Lordships' opinion. It is agreed that one of them involves a point of law, although the two sides differ as to the form in which it may be expressed. As to the other, we think with the Commissioner that it is purely a question of fact and does not arise for reference.

3. The reference is concerned with an assessment to income-tax made upon the applicant in his capacity as the 'karta,' *i.e.*, manager of his Hindu undivided family, for the charge year 1942-43. His 'previous' year, *i.e.*, the year of account, is the year according to the Hindu calendar, so that the income that is assessed is of a period from 31st October 1940 to 20th October 1941. The income is derived from two assessable heads, 'Business' and 'Property.' The Income-tax Officer determined the total income at Rs. 48,559. In appeal, the Appellate Assistant Commissioner reduced it to Rs. 39,733 after permitting certain deductions which are not material. Except for this modification, he sustained in principle the assessment made upon the applicant in the particular legal character. Copies of the Income-tax Officer's and the Appellate Assistant Commissioner's orders are Exhibits C and D.

4. The following is an agreed statement of facts. The assessee family consisted of the applicant, his wife, and six sons, three youngest of whom were minors at the material time. It was a Hindu undivided family, at any rate till the end of July 1941, and the applicant was its 'karta' or manager. The family possessed lands and buildings as well as cash and jewellery. Besides it was carrying on two grocery businesses, one exclusively its own and another in partnership, and several other businesses on commission agency basis in cement, tea and petroleum. All these businesses were carried on by the members of the undivided family as such, the capital invested in all of them being the capital of the family.

5. In July 1941, the members decided to separate and make a partition of the family properties and assets. For that purpose they divided themselves into four groups, the first consisting of the applicant, his wife and three minor sons together, and the remaining three of the respective major sons and their own families. They started making a division of the family cash, jewellery and the businesses, and completed it on July 30, 1941. The division is embodied in a memorandum which they made that day. The document expressly states, and the fact was also admitted before us, that the shares of the different groups in the movables and the businesses did not correspond exactly with the interest that each possessed in the family estate according to Hindu law. It appears that there was some disagreement among the members as regards the division of the immovable properties and

consequently it was agreed that it should be referred to arbitration, and that a final adjustment of the shares should be made by the arbitrators at the time of the division. The memorandum which we have read also sets out these facts.

6. Next day, *i.e.*, July 31, 1941, the parties submitted a reference to arbitration in accordance with the agreement. On October 16 following, the arbitrators made an award dividing the immovable properties and also adjusting the shares of the different groups. The award passed into a civil Court's decree on February 3, 1942.

7. After the division of the businesses on July 30, 1941, the applicant and his three major sons separately carried on those that were assigned to their respective shares till the end of the year of account, *i.e.*, 20th October 1941. But no new books were opened for that period and the family books commenced at the beginning continued to be maintained till the end of the account year.

8. On March 12, 1942, the applicant applied to the Income-tax Officer to record an order of partition, under Section 25A (1) of the Act. In particular, it appears that he asked that the partition as far as it affected the family businesses should be considered to have been made on July 30, 1941, and given effect to from that date. After making the necessary enquiry the Income-tax Officer passed an order recording the partition as on the date of the award, *i.e.*, 16th October 1941. He held that the division and assignment of the several businesses to the different members on July 30 preceding was only a partial partition, and not a complete partition such as the one contemplated by Section 25A (1) of the Act; and that the partition must be considered to have been effected on the date of the award. In appeal, the Appellate Assistant Commissioner took the same view. Copies of the respective orders are Exhibits E and F. The applicant did not take any further appeal to the Tribunal from these orders.

9. The contention was revived in the present assessment for 1942-43, before the Appellate Assistant Commissioner who however dismissed it in view of his earlier order (Exhibit F) just referred to. Thereafter, the applicant took an appeal to the Tribunal (R. A. A. No. 102-Bombay, 1943-44) giving rise to this reference.

10. As stated before, the assessment has been made upon the applicant as the manager of his Hindu undivided family. As a matter of fact, however, the undivided family was not in existence as such at the time of making the assessment, and that is common ground. In such a case, that is to say, when an undivided Hindu family which had received income in the year of account is no longer in existence as such at the time of making the assessment, the

ssessment is to be under Section 25A of the Indian Income-tax Act. ub-section (1) of that section deals with the Income-tax Officer's ower to record an order of partition when any member of Hindu family that had been assessed as undivided claims that a partiion has been effected. If the Income-tax Officer is satisfied that the roperty of the family is partitioned in definite portions among its ifferent members or groups of members he has to make an order reording such partition. Then sub-section (2) of Section 25A describes he manner in which an assessment is to be made upon a family which vas undivided in the year of account and received income as such, but s no longer in existence as an undivided family at the time of making he assessment. In such a case the Income-tax Officer has to compute he total income and determine the amount of tax payable upon it, as if o partition had taken place. Thereafter, he has to apportion the amount f the tax among the different members according to the portions of the amily property allotted to their respective shares, making them jointly nd severally liable to pay the whole of the amount of tax. That is what he Income-tax Officer did in this case. According to the view of the ncome-tax authorities, the applicant's undivided family as such had eceived the income till the end of the previous year, *i.e.*, October 20, 1941, although that family was no longer in existence at the time f making the assessment. He accordingly assessed the whole of the inome of the previous year in the hands of the applicant as the manager r 'karta.' Here a small fact may be explained. The award was made n October 16, and the account year ended four days later, *i.e.*, October 20, 1941. But there is no contest as to the income of that short period as pointed out in our judgment. The Income-tax Officer however appears to have overlooked the provision as to the apportionment of the amount of tax among the different members, but we directed that such an apportionment be made.

11. The applicant's case before us was that the income from the different businesses that were assigned to the several members on July 30, 1941, was not assessable in his hands in the capacity of 'karta' of the undivided family. That is to say, he asked that the income from July 30 to October 20, 1941, should be excluded from his assessment. The learned advocate divided his argument on this point into two parts. In the first place, he contended that a division of the businesses must be taken to have been made on the date of the memorandum, *i.e.*, July 30, and not on October 16, when the partition was completed by the award. So that the income from businesses from the date of their division onwards was not the income received by the Hindu undivided family as such. Secondly, and, in the alternative, he argued

that even if the family partition is taken to have been made on October 16, 1941, the making over of the several businesses to the three major sons in virtue of the division of July 30 amounted to the Hindu undivided family's parting with some of its assets in favour of its own members, so that the Hindu undivided family was no longer in possession of those assets, and, consequently, could not be taxed in respect of the latter. On the first point we held that the division of the businesses on July 30, 1941, was only a stage in the process of partition completed later and could not be regarded as a complete partition by itself. We drew support for our view from *Medam Gurumurthi Setty* v. *Commissioner of Income-tax, Madras,* later reported in [1944] (12 I.T.R. 176). In support of his second point the learned advocate relied upon some of the observations of the Privy Council in *Sir Sundar Singh Majithia* v. *Commissioner of Income-tax, C. P. and U. P.*[1], which we thought was distinguishable from the present one. Our reasons on the first point are recorded in paragraphs 4 and 5 and, on the second, in paragraph 6 of our judgment, a copy of which is Exhibit G.

12. While arguing the present application the learned advocate conceded the first of the two points and did not question our finding as to the date on which the partition should be taken to have been made. He added that it was not necessary to refer any question on that point. He however laid stress on the second point and has formulated a question as below :—

"Whether the income from the several businesses amounting to Rs. 39,733 has been rightly included in the income of the appellant for the purposes of assessment to income-tax."

13. We are afraid that the question does not express the point involved with precision, and, on the contrary, is likely to create a good deal of misunderstanding. In the first place, the amount of Rs. 39,733 is not income from businesses alone. It is total income and includes income from property which had admittedly remained undivided till the date of the award and the income from which had been received by the family till that date. Speaking of the businesses, the income therefrom till the date of their division on July 30, 1941, was admittedly joint family income. In the course of his argument in appeal the learned advocate for the applicant expressly stated that his objection was to the income from the different businesses between July 30, 1941, and the end of the year of account, *i.e.*, October 20, 1941, being included in the assessee family's total income. Thus that portion of the income alone was sought to be excluded from the assessee's assessment. Moreover, one of the

(1) (1942) 10 I.T.R. 457.

businesses, and probably the main business which is the kirana business, was taken over by the 'karta' Mr. Waman Satwappa for his own group. Therefore, should their Lordships accept the applicant's contention a direction for an apportionment will have to be given without which it would be impossible to ascertain the income derived by the different members between July 30, 1941, and October 20, 1941, from the different businesses allotted to their respective shares. The question as it is framed by the applicant might mean that he objects to the whole of the assessment since the income of Rs. 39,733 is the total income. That, however, is not so. Therefore, in order to express the assessee's contention with precision we would frame the question as below.

14. But before doing so, we must dispose of the second question raised by the applicant which is :—

'Whether the Income-tax Officer is right in estimating the gross profit in respect of kirana (grocery) business.'

We agree with the Commissioner in thinking that this is purely a a question of fact. The facts before us were that the applicant had maintained no stock-books nor any details of cash sales. And, consequently, the true profits could not be ascertained from the method of accounting. We therefore held that the Income-tax Officer had no alternative except to estimate them which he did under the proviso to Section 13 of the Act. There was thus material before us to arrive at the finding of fact. In sub-paragraph (7) of paragraph 3 of the reference application, the applicant tries to connect our finding of fact with that on the point of partition by commencing the sub-paragraph with 'In these circumstances' as if the circumstances had any connection with the considerations arising in the decision of the question of partition. We doubtless stated 'In these circumstances' in the concluding paragraph of our judgment, but the contest is altogether different as just pointed out. We therefore think that the second question does not arise for reference being purely a question of fact.

15. Accordingly, we submit the following question for their Lordships' opinion :—

Question referred.

'Whether in the circumstances of the case and having regard to the provisions of Section 25A of the Indian Income-tax Act, 1922, the profits and gains of the several businesses for the period from July 30, 1941, to October 20, 1941, have been rightly included in the total income of the Hindu undivided family represented by the applicant, for the assessment year 1942-43 ?' "

Y. P. Pandit, for the assessee.

M. C. Setalvad, for the Commissioner.

JUDGMENT.

KANIA, AG. C. J.—This is a reference made under Section 66 (1) of the Indian Income-tax Act by the Income-tax Appellate Tribunal.

The relevant facts as found in the statement of case are these. The year of assessment is 1942-43 and the income of the previous year, which is sought to be taxed, is the Hindu year commencing from 31st October 1940 and ending on 20th October 1941. The assessee was sought to be assessed as the karta of a joint Hindu family. He had been so assessed in the previous years. In July 1941 the members decided to separate and make a partition of the family properties and assets. For that purpose they divided themselves into four groups. The first group consisted of the assessee, his wife and three minor sons together. The remaining three groups consisted of the three major sons and their own families. They started making a division of the family cash, jewellery and the businesses and completed it on 30th July 1941. That division was embodied in a memorandum which the parties executed that day. The document expressly stated, and the fact was also admitted before the Tribunal, that the shares of the different groups in the movables and businesses did not correspond exactly with the interest which they possessed in the family estate according to Hindu law. It appears that there was some disagreement amongst the members as regards the division of the immovable properties and consequently there was a reference to arbitration so that the final adjustment of the shares should be made by the arbitrators at the time of the division. On 31st July 1941 the parties submitted a reference to arbitration and the award was made on 16th October 1941. Thereafter a decree on the award was passed on 3rd February 1942.

In paragraph 7 of the statement of case it is stated as follows:— "After the division of the businesses on July 30, 1941, the applicant and his three major sons separately carried on those that were assigned to their respective shares till the end of the year of account, *i.e.*, 20th October 1941." On 12th March 1942 the applicant applied to the Income-tax Officer to record an order of partition under Section 25A (1) of the Act. The order was made on 30th July 1942. The assessee at first claimed that the income of the joint family for the whole year under the circumstances should not be assessed as such but the individual members only should be assessed. In the alternative he claimed that the income of the businesses between 30th July and 20th October should be treated as separate income. The Tribunal rejected the larger contention but has referred for the Court's opinion the

narrower question in respect of the profits of the several businesses between 30th July and 20th October 1941 in the following terms :—

"Whether in the circumstances of the case and having regard to the provisions of Section 25A of the Indian Income-tax Act, 1922, the profits and gains of the several businesses for the period from July 30, 1941, to October 20, 1941, have been rightly included in the total income of the Hindu undivided family represented by the applicant, for the assessment year 1942-43 ?"

The material facts therefore are that according to the findings of the Tribunal the businesses were at one time joint family businesses, they were allotted to the individual members on 30th July 1941, and the assessee and his three major sons thereafter separately carried on those businesses which were assigned to their respective shares till the end of the year. It also appears that the immovable properties belonging to the family were not allotted to individual members and the shares therein were not specifically defined. The value of the movables and the businesses divided on 30th July 1941 were unequal and they had to be equalised at the time of the division of the immovable properties. The Tribunal was of the opinion that there can be only one partition under Hindu law and therefore in the present case as there was no completed partition till the 16th October 1941 the assessee was liable to be assessed for the whole year on the footing that he was the karta of the joint family.

On behalf of the assessee it is contended that the Tribunal has taken a wrong view. It is urged that there is nothing in law to prevent a Hindu family from parting with one or more of its assets in favour of a stranger or a member. If that is done, that particular asset ceases to be a joint family property and the income, profits and gains of such asset in no event can be considered to be that of the joint family. It is contended that the assessment of the karta is and can only be in respect of the income of the joint family properties. In *Sir Sundar Singh Majithia* v. *Commissioner of Income-tax*[1], it is pointed out that Section 25A deals with the position of a joint family which was in existence when the income of the joint family property was received but was not in existence at the date of the assessment. The law therefore provides that in such a case if the joint family has been divided and the properties have been partitioned amongst the various members in definite proportions, the Income-tax Officer can pass an order under Section 25A (1) and thereafter the assessment will be on the individual members only and not on the manager as representing the family. In Section 14 (1) it is therefore provided that tax shall not be payable by the assessee in respect of any sum which he receives

(1) (1942) 10 I.T.R. 457.

as a member of an undivided Hindu family. This is obviously with a view to avoid double taxation. On behalf of the assessee our attention was drawn to *Bansidhar Dhandhania* v. *Commissioner of Income-tax*[1], where the Court held that if businesses were allotted to individual members when the immovable properties had not been partitioned, the income of the businesses did not form part of the income of the joint family for which the karta could be assessed as before. The assessee further relied on the above-mentioned judgment of the Privy Council in *Majithia's case*[2].

On behalf of the Commissioner it is urged that *Majithia's case*[2] is not applicable because in that case the family had continued to be joint and it was only one asset which had been taken out of the family properties and treated by agreement between the parties as a partnership asset. It was contended that the observations in that case were inapplicable when the family unit had been disrupted although there had been no partition of the family assets. Mr. Setalvad further relied on *Medam Gurumurthi Setty* v. *Commissioner of Income-tax*[3], in support of the contention that the partition contemplated by Section 25A means a complete partition and not a partial partition. It was contended that if in the course of division of the joint family assets some assets are handed over to individual members, till an order under Section 25A (1) is made, the manager continues to be liable to be assessed with the "status" of the "joint undivided Hindu family." He urged that the scheme of Section 25A negatived the contention of the assessee.

In my view, the contention of the assessee is correct. In *Majithia's case*[2], the Board held that it was open to the members of a joint Hindu family to separate one of its assets, so as to make it not to belong to the joint family and in respect of which they can enter into an agreement of partnership. If that asset was a business the income derived from carrying on such a business thereafter would not form part of the joint family income and Section 25A would not come in the way of such an arrangement. This is in accordance with the ordinary rule that there is nothing in Hindu law to prevent individual members from holding separate property. In such a case the member will be liable to be taxed on his separate income. In respect of the joint family income however the manager will be liable to pay the tax as the karta. It must be remembered that Section 25A is a machinery section. It is not a charging section much less it can be construed as altering the Hindu law as such. Mr. Setalvad's argument that that line of reasoning cannot apply when the joint family status has come to an end does not appeal to me. There appears no reason why in the course of partition, which may take five to ten years if the immovable properties are not capable of being easily sold, the members

(1) (1944) 12 I.T.R. 126. (2) (1942) 10 I.T.R. 457. (3) (1944) 12 I.T.R. 176.

should not be given the movables which become their absolute property from the moment they are so given to them individually, so that they can deal with them according to their absolute discretion and right and which is under their absolute domain. The income of such assets so irrevocably transferred to each member is his individual income with which the joint family has nothing to do. If such an arrangement can be arrived at when the joint family is in existence there is nothing in law to prevent the same being done in the course of partition of a joint family. The question whether it has been so done is a question of fact, but in law I find nothing to prevent such a thing being done.

In *Medam Gurumurthi Setty* v. *Commissioner of Income-tax*[1], the question submitted for the Court's opinion was this: "Whether the partition could be said to have taken place within the meaning of Section 25A on 15th October 1938 when the members began to live separately though all the properties were not divided." It must be noticed that the question was whether on the date mentioned in the question, on the facts, it could be stated that there was a partition within the meaning of Section 25A. The facts mentioned in the report are these: On 15th October 1938 the brothers agreed to separate and on 22nd January 1941 a deed of partition was executed and registered. The family estate consisted of immovable and movable properties. On 15th October they divided the cash which they possessed. Each brother was given a house. The other immovable properties were also divided amongst the brothers on that day. On 25th December 1938 they divided the furniture and household utensils. The family had carried on a grocery business but the assets of this business were not divided till 24th February 1939. On these facts the assessee contended that there was a partition within the meaning of Section 25A on 15th October 1938. That contention was rejected. To that extent there is no difficulty in agreeing with the conclusion of the Court. In the course of his judgment the Chief Justice observed: "Partition means a completed partition. The fact that some assets are divided and others are left for division at a future date would not be a partition within the meaning of the section. In this case important assets, namely, those of the business were not divided until February 1939 and the Court has been informed that other assets still remain to be divided. In these circumstances it is clear that the date of the partition is not the 15th October 1938, and that is the answer to give to the reference." While agreeing with the answer given by the Court, with respect, I am unable to agree with the conclusion that Section 25A does not contemplate a division amongst the members of assets of a joint family which can from that moment be their individual property and cease to be the joint family property.

(1) (1944) 12 I.T.R. 176.

On the other hand *Bansidhar Dhandhania's case*[1] relied upon by the assessee brings out the point very clearly. In that case there was a partition and a severance of the joint family status. Businesses were allotted to members and the profits thereof were enjoyed by them individually for their absolute use and benefit. In giving judgment Manohar Lall, J., found as a fact that "the assessee is no longer a joint undivided Hindu family... So far as the businesses are concerned it is impossible to divide them except by sharing of the profits and losses at the close of the year or whenever the accounting comes to be made for the profit and loss of the business of the relevant years." As a fact he found that the accounts were kept separately. It was further found that the house property and the jote lands were not partitioned. He then observed as follows:—"It must, therefore, be held that there is no complete partition but only a partial partition. But such a partial partition comes within the operation of Section 25A of the Act as observed by their Lordships in *Majithia's case*[2] and the Commissioner's view to the contrary is wrong. The members of the assessee's family in these circumstances must be deemed to continue to form a joint Hindu family for the purpose of assessing them on that portion of the income which is derivable from those properties which have not been partitioned in definite portions other than the businesses." The facts there were very similar to the facts here. Businesses were allotted to individual members while the immovable properties remained to be partitioned. The Court there held that the income of the businesses should be treated as the income of the individual members and for that income the joint family cannot be assessed. In my opinion, that is the correct construction of Section 25A of the Act.

Mr. Setalvad further relied on the wording of Section 25A (2). He argued that where an order has been made as contemplated by clause (1) of that section the Income-tax Officer must make the assessment of the total income received by or on behalf of the joint family as such, as if no separation or partition had taken place, and each member or group of members shall, in addition to any income-tax for which he or it may be separately liable and notwithstanding anything contained in sub-section (1) of Section 14, be liable for a share of the tax on the income so assessed according to the portion of the joint family property allotted to him or it. It was argued that it was therefore contemplated by this sub-clause that when there was a rupture of the joint family tie, if the shares were not definitely allotted in individual property to individual members the assessment must continue as before. This contention overlooks the important words found in the clause namely, "on

(1) (1944) 12 I.T.R. 126. (2) (1942) 10 I.T.R. 457.

assessment of total income received by or on behalf of the joint family as such." The essence of the section is that the income must in the first instance be received by the joint family as such. Once it is so received it makes no difference whether the joint family exists or not on the date of the assessment. This section, in my opinion, clearly brings out what was pointed out by the Privy Council in *Majithia's case*[1], that the scheme of the section was to tax joint family income as a unit if it was received as such by the joint family, even though at the date of the assessment there may have been a partition.

It seems to me therefore that there being nothing in Hindu law to prevent members of the joint family owning individual assets at certain stages when the joint family exists or when it is in the course of partition, in the present case, as the businesses were individually allotted and worked by the members separately for their own benefit, as found by the Tribunal, the income in question cannot be considered to be the income of the joint family.

The question referred to the Court must therefore be answered in the negative. The Commissioner to pay the costs of the reference.

CHAGLA, J.—I agree. Section 25A of the Indian Income-tax Act does not create any new rights or obligations nor does it in any way affect the provisions of the Hindu law. The section merely sets up a machinery by which the income of a joint Hindu family, which was in existence in the accounting year but has become defunct in the year of assessment, can be computed and calculated. In Hindu law when there is severance of joint status the joint family ceases to exist as an entity although the properties are not partitioned. As far as the Income-tax Act is concerned the joint family, although its status has been severed, continues to exist as a unit or entity till all the properties belonging to the joint family are completely and finally partitioned. To my mind the scheme of Section 25A is very clear. It is only when not only the status is severed but also all the properties have been partitioned that the order contemplated by Section 25A (1) can be applied for and made, and till such an order is made, for the purposes of income-tax, the joint family continues to exist as a unit although its status may have come to an end. Sub-clause (2) provides for the mode of assessment after the order has been made. It provides that after the order has been made as contemplated by the first sub-clause the tax has got to be apportioned to the shares of the different members of the joint family but the tax has got to be assessed on the total income received by the joint family or on behalf of it. But what has got to be remembered is that under sub-clause (2) of Section 25A what has got to be assessed is the total income of the joint family. Therefore in every case the Income-tax authorities have to ascertain what is the total income of the joint

(1) (1942) 10 I.T.R. 457.

family. It is true that although the joint family has ceased to exist in the eye of the Hindu law still it may continue in the eye of the Income tax Act, and till all the properties have been partitioned the income received by the karta from the properties still not partitioned will still be the income of the joint family. But all the same it must be found as a fact that the joint family as recognised by the Income-tax Act has received the income which is sought to be assessed. Therefore, to my mind, the question in this case resolves itself into a question of fact *viz.*, is the income of the business which according to the Income-tax authorities is a part of the total income of the joint family and was assessed under sub-clause (2) income of the joint family or not? On this the clear and specific finding of fact is that after the 30th July 1941 the three major sons and their family carried on their own businesses separately and they were the owners of those businesses. Now Mr. Setalvad's contention is that once a joint family becomes disrupted till the final partition takes place all its assets must be deemed to be the assets of the joint family and all the income received must be deemed to be the total income of the joint family. Now in my opinion there is no warrant for that proposition. There is nothing in Hindu law to prevent the members of a joint family which has become disrupted from parting with the assets either to a stranger or to one of themselves. In the Privy Council case (*Majithia's case*[1]) their Lordships were considering the case of a joint and undivided Hindu family which had merely divided some of its assets, and Sir George Rankin in delivering the judgment of the Board points out that there was no warrant in reading in Section 25A a prohibition that members of a joint and undivided Hindu family cannot part with some of their assets to a stranger or to one of themselves. I find even less warrant for reading in Section 25A a prohibition that members of a family which in Hindu law was joint and undivided but which has ceased to be a joint and undivided family cannot part with assets of that separated joint family either to a stranger or to one of themselves. I agree with the learned Chief Justice that the facts in the Patna case (*Bansidhar Dhandhania* v. *Commissioner of Income-tax*[2]), are practically undistinguishable from the facts before us. There the learned Judges found as a fact that the assessee whose case they were considering was no longer a joint and undivided Hindu family. They held that whereas the businesses had been partitioned the house property and the jote lands had not been partitioned and they came to the conclusion that there was no completed partition but only a partial partition and they further held that such a partial partition came within the operation

(1) (1942) 10 I.T.R. 457. (2) (1944) 12 I.T.R. 126.

of Section 25A of the Act. The effect of their finding was that as there was not a complete partition but only a partial partition a Hindu family must be considered to be joint for the purposes of the Income-tax Act to the extent of those assets which had not been partitioned. In other words, the Hindu family must still be considered as a unit for the purposes of the Income-tax Act to the extent the family had retained the property which had not been partitioned. To the extent it had parted with the assets the finding of the Court is clear that those assets can no longer be considered to be the assets of the family or forming part of the total income of the family or that the family was liable to pay tax thereon under Section 25A (2). Under the circumstances I agree with the learned Chief Justice that we must answer the question referred to the Court in the negative, and the Commissioner should pay the costs of the reference.

Reference answered in the negative.

[IN THE MADRAS HIGH COURT.]

COMMISSIONER OF INCOME TAX, MADRAS

v.

MOTORS AND GENERAL STORES LTD.

SIR LIONEL LEACH, C. J., and PATANJALI SASTRI, J.

January 18, 1946.

INDIAN INCOME-TAX ACT (XI OF 1922), SEC. 10 (2) (vi), SEC. 10 (3) —DEPRECIATION ALLOWANCE—MACHINERY USED ONLY FOR PORTION OF PREVIOUS YEAR—WHETHER DEPRECIATION FOR WHOLE YEAR CAN BE ALLOWED—SEC. 10 (3), SCOPE OF.

The assessee company carried on business in electrical stores and in the distribution of electricity during the whole of the year of account and also carried on for two months and seven days before the close of the year an oil mill business. The Income-tax authorities held that as the oil mill had only worked for a portion of the previous year, the assessee was not entitled to the full allowance for depreciation under Section 10 (2) (vi) of the Income-tax Act, but was only entitled to a proportionate allowance :

Held, *that the assessee was entitled to a depreciation allowance under Section 10 (2) (vi) for the whole period of the previous year.*

Section 10 (3) only makes provision to meet a situation where the machinery is used in part for the business of the assessee and in part for other purposes. The word " wholly " does not mean wholly throughout the year.

Case referred to :—

Indian Iron & Steel Co., Ltd. v. Commissioner of Income-tax, Bengal [1943] (11 I.T.R. 328 ; 208 I.C. 434 ; 48 C.W.N. 52 ; A.I.R. 1943 P.C. 124 ; I.L.R. 1943, 2 Cal. 524).

Case referred to the High Court by the Income-tax Appellate Tribunal under Section 66 (1) of the Indian Income-tax Act, 1922 (Act XI of 1922), as amended by Section 92 of the Income-tax (Amendment) Act, 1939 (Act VII of 1939), in Application No. 66 R.A. No. 49 (Madras) of 1944-45 (Assessment year : 1942-43) on its file for decision of the question of law mentioned in para. 1 of the Statement of Case: Case Referred No. 17 of 1945.

STATEMENT OF CASE.

" This is an application by the Commissioner of Income-tax, Madras, asking us to refer the following question of law for the opinion of the Honourable High Court at Madras :—

' Whether on the facts and in the circumstances of the case when the assessee actually used the plant and machinery for the purposes of his business in the previous year only for a period of two months and seven days, the assessee can be granted a depreciation allowance under Section 10 (2) (vi) for the whole period of the previous year in question ? '

The application arises out of the Tribunal's order, dated 7th July 1944, in R.A.A. No. 188 (Madras) of 1943-44.

2. The facts of the case are as under :—

The respondent is a limited company whose assessed income for the assessment year 1942-43 was nil and the allowance of depreciation carried forward was determined at Rs. 55. The respondent company claimed that the depreciation to be carried forward should be determined at Rs. 2,991. These figures will be considered later. The respondent company carried on certain businesses during the whole of the relevant accounting year, but they started a new business which may be called groundnut oil expeller business on 23rd January 1942, *i.e.*, two months and seven days before the close of the year. The businesses which were conducted throughout the year were :—

(1) trade in electrical general stores ; and

(2) distribution of electricity.

The net income of business (1) was finally determined at Rs. 329 and that of (2) after deducting a full year's depreciation at Rs. 403 ; the total income of the two businesses thus came to Rs. 732. The new business of groundnut oil expulsion returned a loss of Rs. 3,724 including depreciation of Rs. 3,614. The Income-tax Officer, eliminating depreciation, determined the loss at Rs. 110, deducted the same from

the other income of Rs. 732 and arrived at a net income of Rs. 622. As regards depreciation of the new business he calculated the total depreciation for the year at Rs. 3,613, but allowed a proportion for two months and seven days only. This came to Rs. 677 which was set off against the income of Rs. 622 referred to above and the balance of Rs. 55 was carried forward to be set off against subsequent year's income. The respondent company claimed that although the new business ran for two months and seven days only there was nothing in the Act which precluded them from claiming a full year's depreciation. The allowance for depreciation is governed by Section 10 (2) (vi) of the Act and looking to the language of the section the Tribunal decided in favour of the respondent company. The Tribunal has given its reasons for arriving at such a decision in their order under Section 33 (4) of the Act (Exhibit T-E).

3. Although the respondent company states that there is no question of law, we are of opinion that a question of law does arise and we are referring the question suggested by the applicant and cited hereinabove for the opinion of the Honourable High Court."

C. S. Rama Rao Saheb, for the Commissioner.

T. V. Viswanatha Ayyar, for the assessee.

JUDGMENT.

LEACH, C. J.—The assessee is a limited liability company. During the whole of the year of account (1942-43) it carried on business in electrical stores and in the distribution of electricity. For part of the year, namely, from the 23rd January, 1942, to the 31st March, 1942, it also carried on an oil mill business. Although the oil mill had only worked for two months and seven days in the year of account, the company claimed to be entitled to deduct the full allowance for depreciation contemplated by Section 10 (2) (vi) of the Income-tax Act. The Income-tax Officer held that the company was only entitled to a proportionate allowance and this decision was accepted by the Appellate Assistant Commissioner. On appeal by the assessee to the Income-tax Appellate Tribunal, the decision of the Appellate Assistant Commissioner was reversed. The Tribunal held that on the wording of the section, the assessee was entitled to an allowance as if the machinery had been worked throughout the year.

At the instance of the Commissioner of Income-tax, Madras, the Tribunal has, under Section 66 (1) of the Act, referred to this Court the following question :—

" Whether on the facts and in the circumstances of the case when the assessee actually used the plant and machinery for the purposes of

his business in the previous year only for a period of two months and seven days, the assessee can be granted a depreciation allowance under Section 10 (2) (vi) for the whole period of the previous year in question?"

While conceding that there is no indication in clause (vi) of sub-section (2) of Section 10 that the allowance for depreciation is dependent on a time factor and that if the clause stood alone the assessee would be entitled to the full allowance, Mr. Rama Rao Saheb on behalf of the Commissioner says that sub-section (3) of Section 10 and sub-section (2) of Section 26 govern the clause and make it necessary to read it as the department has read it.

We can find nothing in sub-section (3) of Section 10 or in sub-section (2) of Section 26 to support this argument. Sub-section (3) of Section 10 reads as follows:—

"Where any building, machinery, plant or furniture in respect of which any allowance is due under clause (iv), clause (v), clause (vi) or clause (vii) of sub-section (2) is not wholly used for the purposes of the business, profession or vocation, the allowance shall be restricted to the fair proportional part of the amount which would be allowable if such building, machinery, plant or furniture was wholly so used."

This sub-section only makes provision to meet a situation where the machinery is used in part for the business of the assessee and in part for other purposes. In this case the machinery of the oil mill was used wholly for the assessee's business. The word "wholly" does not mean wholly throughout the year. Clearly sub-section (3) cannot deprive the assessee of what he is entitled to under clause (vi) of sub-section (2). Section 26 (2) is merely a provision to meet the case where a person carrying on a business, profession or vocation is succeeded in the course of the year of account by another person who carries on the same business, profession or vocation. The Privy Council pointed out in *Indian Iron & Steel Co., Ltd. v. Commissioner of Income-tax, Bengal*[1], that this sub-section (2) of Section 26 is not concerned with the computation of tax, but with the person upon whom the liability is imposed. When one wants to compute what is payable by way of tax, one has to go to Section 10.

Mr. Rama Rao Saheb has suggested that the judgment in this case supports his argument, but we do not agree. There the appellant company had taken over the business of another company as and from the 2nd December 1936. The company whose business was taken over had worked at a loss and its unappropriated depreciation

(1) (1943) 11 I.T.R. 328; I.L.R. [1943] 2 Cal. 524.

allowance stood at a very large figure. The contract between the two companies contained a clause assigning to the appellant company, so far as was capable of being assigned, any claim which the old company had in respect of unabsorbed depreciation allowance. By virtue of this assignment, the appellant company claimed to be entitled to set off against its profits the unabsorbed depreciation allowance of the old company, but the Privy Council held otherwise. This was the sole question in the appeal. The question now before us was not even raised before their Lordships. Inasmuch as their Lordships did hold that Section 26 (2) as it was before its amendment was not concerned with the computation of tax, their judgment, if anything, is against the argument now advanced on behalf of the Commissioner.

We hold that the Income-tax Appellate Tribunal rightly decided the case and consequently answer the question referred in the affirmative. We may add that this interpretation of the section will not affect the Income-tax authorities detrimentally. The depreciation can only be allowed to the extent of the cost of the machinery and the allowance of the full amount for the year of account will mean that the benefit conferred on the assessee by Section 10 (2) (vi) will be more quickly worked out. The Commissioner must pay the costs of the assessee, Rs. 250.

Reference answered in the affirmative.

[IN THE PATNA HIGH COURT.]

COMMISSIONER OF INCOME-TAX, BIHAR AND ORISSA

v.

SRIMATI CHANDRAMONI PATTAMAHADEVI RANI SAHEBA.

FAZL ALI, C.J., and MANOHAR LALL, J.

January 9, 1946.

INDIAN INCOME-TAX ACT (XI OF 1922), SEC. 14 (1)—EXEMPTIONS —"SUMS RECEIVED AS MEMBER OF HINDU UNDIVIDED FAMILY"—IMPARTIBLE ESTATE—MAINTENANCE ALLOWANCE PAID UNDER DEED TO WIDOW WHO SURRENDERED RIGHTS IN ANOTHER ESTATE—WHETHER EXEMPT.

A junior member of the Jeypore family (an impartible estate) married a lady belonging to the Madgole family and they had a son K. Under a compromise decree K's son established his rights to a half share of the Madgole estate and to the ownership of the other half share also after the death of a widow. After the death of K's son, his widow, the assessee, and her mother-in-law executed a deed in favour of the Maharaja of Jeypore providing that after the death of the executants the Madgole estate should devolve upon the Maharaja. Later on the assessee (her

mother-in-law having died in the meantime) executed another deed by which she surrendered, conveyed and assigned to the Maharaja the entire Madgole estate and the latter agreed to pay to the assessee monthly a sum of Rs. 1,650 as maintenance and residence allowance. This sum was made a first charge on the Madgole estate: Held, *that even assuming that the assessee was joint with the Maharaja to whom she had surrendered the estate the sum of Rs. 19,800 which she received annually under the deed was not a sum received by her as member of a Hindu undivided family within the meaning of Section 14 (1) of the Indian Income-tax Act and was not exempt from tax under that section.*

The unfailing test for the applicability of Section 14 (1) in such cases is to determine whether the allowance would cease if the assessee ceased to be a member of the family.

Shrimati Maharani Laxmipat Mahadevi Garu Dowager Maharani of Jeypore v. *Commissioner of Income-tax, U. P. and C. P.* [*1944*] (*12 I.T.R. 489*) followed.

Commissioner of Income-tax v. *Maharani Gyan Manjuri Kuari* [*1945*] (*13 I.T.R. 55 ; I.L.R. 24 Pat. 159*) and *Commissioner of Income-tax, C.P. and U.P.* v. *Rani Rudh Kumari* [*1940*] (*8 I.T.R. 607*) distinguished.

Cases referred to :—

Baijnath Prasad Singh v. Tej Bali Singh [1921] (48 I.A. 195).

Commissioner of Income-tax, Punjab v. Dewan Bahadur Dewan Krishna Kishore [1941] (9 I.T.R. 695 ; 68 I.A. 155 ; 196 I.C. 707 ; A.I.R. 1941 P.C. 120 ; I.L.R. 1942 Lah. 1).

Commissioner of Income-tax v. Maharani Gyan Manjuri Kuari [1945] (13 I.T.R. 55 ; I.L.R. 24 Pat. 159).

Commissioner of Income-tax, C.P. and U.P. v. Rani Rudh Kumari [1940] (8 I.T.R. 607).

First Pittapur Case (Venkata Rao v. Court of Wards) [1899] (26 I.A. 83 ; 22 Mad. 383).

Gorakhpur Case (Collector of Gorakhpur v. Ram Sunder Mal) [1934] (61 I.A. 286 ; I.L.R. 56 All. 468 ; 150 I.C. 542 ; A.I.R. 1934 P.C. 157).

Jeypore Case (Vikram Deo Maharajulum Garu Maharajah of Jeypore v. Vikrama Deo Garu) [1919] (24 C.W.N. 226).

Kartar Singh v. Commissioner of Income-tax, Punjab [1937] (5 I.T.R. 269).

Sartaj Kuari v. Deoraj Kuari [1888] (I.L.R. 10 All. 272).

Second Pittapur Case (Raja Rama Rao v. Raja of Pittapur) [1918] (I.L.R. 41 Mad. 778 ; 45 I.A. 148).

Shibaprasad Singh v. Prayag Kumari Debee [1932] (59 I.A. 331 ; I.L.R. 59 Cal. 1399).

Shrimati Maharani Laxmipat Mahadevi Garu Dowager Maharani of Jeypore v. Commissioner of Income-tax, U.P. and C.P. [1944] (12 I.T.R. 489).

Tipperah Case [1869] (12 M.I.A. 523 ; 3 B.L.R.P.C. 13).

Reference under Section 66 (2) of the Indian Income-tax Act (XI of 1922) by the Income-tax Appellate Tribunal : (Miscellaneous Judicial Case No. 33 of 1944).

STATEMENT OF CASE.

"In pursuance of the High Court's order, dated the 21st August 1944, the following statement of the case is submitted :—

The respondent to this application is the widow of late Mukund Dev, adopted son of Krishna Dev, who got the property of the

impartible estate of Madgole as the daughter's son of the late Lunga Bhupati Dev who was the last male holder of that estate in his line. This Krishna Dev was also a member of the Kalyanpur branch, a junior branch of the Jeypore family who owned another impartible estate, the Jeypore. The members of the family of the owners of Madgole estate and Jeypore estate were related only by this marriage of the father of Krishna Dev to the daughter of the late Lunga Bhupati Dev.

The two estates of Jeypore and Madgole are both governed by the Madras Impartible Estates Act, 1904, and both these estates are mentioned in the schedule annexed to the Act. The Madras Impartible Estates Act enacts that maintenance will be granted to certain persons mentioned therein. The husband of the respondent was a member of the Kalyanpur branch of the family owning the Jeypore estate and as it was not shown that the husband had become divided it was held relying on the presumption of law and the reasons given in our order that the respondent's husband continued to be a member of the joint Hindu family owning the impartible Jeypore estate.

By a registered document between the respondent and her mother-in-law on one side and the late Maharaja Vikram Dev, K.C.I.E., Maharaja of Jeypore and Sri Ramchandra his son on the other it was agreed that on the death of the two ladies the Madgole estate should pass to the Maharaja of Jeypore and his son. Before the 28th June 1928 on which date the respondent to this application surrendered the widow's estate to the Maharaja of Jeypore, Maharaja Vikram Dev had passed away and the widow surrendered the widow's estate to the nearest reversioner Sri Ramchandra Dev, the then Maharaja of Jeypore. It was recited in the said deed that by law and custom of lineal primogeniture obtaining in the Madgole estate the Maharaja was the reversioner. By the said document the Maharaja of Jeypore on his part agreed in lieu of the estate surrendered by the respondent to provide a suitable maintenance and residence to her, but no other benefits, whatsoever, were reserved in her favour.

This Tribunal held that by the Madras Impartible Estates Act of 1904 as amended in 1934 the holder for the time being is the individual owner of the property but the other members of the family have the right of reversion and chances of succession in the properties and the junior members are entitled to maintenance and the widow of the last holder of the estate is also one of the persons entitled to maintenance. After referring to the several authorities mentioned in the order under Section 33 the Tribunal reached the conclusion that the allowance for the maintenance and

residence was made to the widow as a member of the joint family which owned the Madgole estate and this payment was governed by Section 14 (1) of the Income-tax Act and as such was not liable to income-tax.

The questions raised by the applicant are: (1) Whether in the circumstances of the case the sum of Rs. 19,800 received by the assessee from the Maharaja of Jeypore is exempt from income-tax under Section 14 (1) of the Income-tax Act? (2) Whether the Madras Impartible Estates Act, 1904, as amended in 1934, has any application to the facts and circumstances of the case?

The decision of the Tribunal has been based on the ground that the Madras Impartible Estates Act, 1904, as amended in 1934, is applicable to the Jeypore and Madgole estates. Hence it is desirable that this question is put first. Then the question whether the sum of Rs. 19,800 received by the respondent, 18,000 for maintenance and 1,800 for residence, is received as a member of the Hindu undivided family will follow. The reasons for holding that the Madras Impartible Estates Act of 1904 as amended in 1934 does apply and the reasons for holding that she is the member of the family which owned the Madgole estate are stated fully in the order of the Tribunal.

On another ground it was held that the amount received by the respondent would be exempt from taxation. If it was considered that the widow did not surrender her whole estate to the reversioner because of the reservation for maintenance and residence, expressly stated in the deed, then she had not parted with her property. If she had not parted with her property then it was obvious that the money received from the Maharaja of Jeypore, the sum of Rs. 19,800, was the income of her own estate paid to her by the manager for the time being and it was agricultural income. Even on that ground under Section 2 (1) the respondent would not have been liable to tax.

The Commissioner of Income-tax, the applicant in this case, submits in paragraph 10 of his application that the above finding was an obiter dictum and in paragraph 12 it is stated that the respondent did not claim exemption under Section 2 (1) of the Income-tax Act at any stage of the proceeding. We must observe that at the time of hearing of the appeal this matter was urged by the advocate of the respondent and it is therefore that the finding referred to by the Commissioner of Income-tax finds a place in the order of the Tribunal under Section 33 of the Income-tax Act.

With this statement of the case the following questions are referred to the High Court of Judicature at Patna for their opinion :—

'(1) Whether in the circumstances of the case the sum of Rs. 19,800 received by the assessee from the Maharaja of Jeypore is exempt from income-tax under Section 14 (1) of the Income-tax Act?

(2) Whether the Madras Impartible Estates Act, 1904, as amended in 1934, has any application to the facts and circumstances of the case?' "

S. N. Dutt, for the Commissioner.

P. R. Das and *G. C. Das*, for the assessee.

JUDGMENT.

FAZL ALI, C. J.—In this reference two questions of law have been referred to us for our opinion, namely :—

"(1) Whether in the circumstances of the case the sum of Rs. 19,800 received by the assessee from the Maharaja of Jeypore is exempt from income-tax under Section 14 (1) of the Income-tax Act ?

(2) Whether the Madras Impartible Estates Act, 1904, as amended in 1934, has any application to the facts and circumstances of the case ?"

It was conceded on behalf of the assessee that the Madras Impartible Estates Act, 1904, as amended in 1934, has no application to the facts and circumstances of this case. Therefore the second question must be answered in the negative.

As to the first question, I shall have to refer to certain facts before answering it. In the appellate order of the Income-tax Tribunal there is a reference to two pedigrees, one of Jeypore family and another of Madgole family. It is common ground that these two families are connected by marriage only. It appears that one Mukund Deo No. 1, a junior member of the Jeypore family, married a lady belonging to the Madgole family who bore him a son named Krishan Deo. After the death of Krishan Deo, a dispute arose between his son Mukund Deo No. 2 the husband of the assessee, and one Rajendramoni Debi, another member of the Madgole family, about the ownership of the Madgole estate. Ultimately there was a compromise by which a small part of the estate was given to Rajendramoni in absolute right and the rest of the estate was divided equally between Mukund Deo No. 2, and Rajendramoni subject to the qualification that Rajendramoni was to enjoy her share of the estate only during her lifetime and upon her death it was to devolve upon Mukund Deo. After the compromise Mukund Deo and Rajendramoni brought a suit against the present Maharaja Ramchandra Deo and the late Maharaja Vikram Deo for the redemption of a mortgage relating to half the estate. Ultimately the parties compromised this dispute and a decree was passed providing for the redemption of the property

upon payment of Rs. 4,40,000. For the payment of this amou: Mukund Deo and Rajendramoni executed a registered sale deed favour of the two Maharajas in respect of half the Madgole esta Upon the death of Mukund Deo the assessee and her mother-in-la executed a registered deed in favour of Maharaja Vikram Deo a Maharaja Ramchandra Deo which provided, among other things, tl upon the death of the two executants and of Rajendramoni, the M gole estate would devolve upon the two Maharajas who were describ as the nearest heirs to the last male holder of the estate. On the 28 June 1928 the assessee (her mother-in-law having died in the mea time) executed a deed by which she "surrendered, conveyed and signed" to Maharaja Ramchandra Deo the entire Madgole est which had been left in her possession as well as the vested remain in that portion of the estate in which Rajendramoni had a life esta Under paragraph 10 of this deed Ramchandra Deo agreed to pay the assessee monthly a sum of Rs. 1,500 as maintenance allowa and a sum of Rs. 150 as allowance for her residence; and under pa graph 12 the total sum of Rs. 1,650 per mensem was made the fi charge on the Madgole estate. In accordance with this agreement assessee received the sum of Rs. 19,800 as allowance in the year account, and thus a question arose as to whether this sum was lia to taxation or was exempt therefrom under Section 14 (1) of the come-tax Act. The view expressed by the Income-tax Officer and Assistant Commissioner of Income-tax was that this sum was taxab but the Income-tax Tribunal held in its appellate order under S tion 33 of the Act that this sum was exempt from taxation. T Tribunal in coming to this decision relied in the first instance on Madras Impartible Estates Act, 1904, which is now conceded to h no application. They also held after referring to a number of decisi relating to impartible property that the sum in question was recei by the assessee as a member of a Hindu undivided family and w therefore, exempt from taxation under Section 14 (1) of the Act. Th held as a fact that the assessee was a member of the Jeypore fam which was a Hindu undivided family and concluded by saying: "I be considered that the appellant has not parted with the property rep sented by the amount of maintenance, it will be agricultural incom

After this decision the Commissioner of Income-tax made an ap cation to the Tribunal asking them to refer the two questions, wh are set out above, to the High Court; but they dismissed the appli tion and while dismissing it they observed as follows: "For the reas stated fully in our said order we held that the widow surrendered right in the property of the Hindu undivided family to the n

male reversioner reserving maintenance to herself, and that the respondent received the amount as a member of the Hindu undivided family and she was entitled to exemption under Section 14 (1) of the Indian Income-tax Act. We further held that if it be considered that the respondent had not surrendered the widow's estate then she had not parted with the property represented by the money received when the receipt will be from her own estate and the income therefore was agricultural and exempt under Section 2 (1) of the Income-tax Act. The decision of the Tribunal was therefore on two alternative grounds and based on the relief admissible under two different sections, 2 (2) and 14 (1). The applicant has now raised questions of law in regard to the first ground whether the amount was received as a member of the Hindu undivided family. The question arising out of the decision we gave that it was not exempt under the provisions of Section 14 (1) (*sic*) it will be exempt under the provisions of Section 2 (1) has not been raised. As this latter finding has become final now any answer on the reference on the first point alone will not disturb the final result of this Tribunal's order. At such a stage the opinion of the High Court will be obtained only on an academic point. We see no justification for making any such reference. We do not therefore propose to refer the questions to the High Court, as being infructuous."

After this order this Court was moved by the Commissioner of Income-tax to direct the Tribunal to submit a statement of the case under Section 66 and hence this reference.

The first point raised by the assessee before us was that in view of the observations of the Tribunal which have been quoted above, question No. 1 becomes academic and it is not necessary for this Court to answer it. On the other hand, it was contended on behalf of the Commissioner of Income tax that the order of the Tribunal made under Section 33 of the Act contains no final decision as to the disputed amount being agricultural income and any observation on the subject made in that order must be regarded as mere obiter. Ultimately both parties agreed that the question which has been referred to us should be answered and the Tribunal should be left to decide hereafter whether notwithstanding our answer the assessee is to be exempted from taxation.

Now, in answering the question, I must proceed on the assumption that the assessee is joint with Maharaja Ramchandra Deo to whom she has surrendered her estate, notwithstanding the fact that the evidence on that point does not seem to be quite complete. In *Commissioner of Income-tax, Punjab* v. *Dewan Bahadur Dewan Krishna Kishore*[1],

(1) (1941) 9 I. T. R. 695.

Sir George Rankin after reviewing most of the earlier decisions of the Privy Council which dealt with the right of the junior member of a joint Hindu family to claim maintenance out of the income of an impartible estate, observed that the law as declared in the cases of *Baijnath*[1] and *Shiba Prasad Singh*[2] has not been unsettled by the *Gorakhpur case*[3]. In view of this expression of opinion, it is necessary to refer to the following observations of Sir Dinshaw Mulla in *Shiba Prasad Singh* v. *Prayag Kumari Debee*[2]: " The keynote of the whole position, in their Lordships' view, is to be found in the following passage in the judgment in the *Tipperah case*[4]. ' Where a custom is proved to exist, it supersedes the general law, which, however, still regulates all beyond the custom.' Impartibility is essentially a creature of custom. In the case of ordinary joint family property, the members of the family have: (1) the right of partition; (2) the right to restrain alienations by the head of the family except for necessity; (3) the right of maintenance; and (4) the right of survivorship. The first of these rights cannot exist in the case of an impartible estate, though ancestral, from the very nature of the estate. The second is incompatible with the custom of impartibility, as laid down in *Sartaj Kuari's case*[5] and the *First Pittapur case*[6]; and so also the third as held in the *Second Pittapur case*[7]. To this extent the general law of the Mitakshara has been superseded by custom, and the impartible estate, though ancestral, is clothed with the incidents of self-acquired and separate property."

In my opinion, therefore, the law on the subject has been correctly summed up in *Shrimati Maharani Laxmipat Mahadevi Garu Dowager Maharani of Jeypore* v. *Commissioner of Income-tax, U.P., C.P. and Berar*[8], in these words: " As regards the right of the widow to maintenance from the holder of an impartible estate it may be regarded as settled law that this rests on custom, and that such custom in the case of younger sons at least has so often been judicially recognised as not to require proof."

It seems to me, however, that the discussion of the general question as to how far a widow is entitled as of right to maintenance out of the income of the impartible estate is not necessary in this case. It is common ground that the allowance which the assessee received in the year of account was paid to her under the deed of the 28th June, 1928. It was pointed out in *Kartar Singh* v. *Commissioner of Income-tax, Punjab*[9], that the unfailing test for the applicability of Section 14 (1)

(1) (1921) 48 I.A. 195.
(2) (1932) 59 I.A. 331.
(3) (1934) 61 I.A. 286.
(4) (1869) 3 B.L.R. P.C. 13 at p. 19.
(5) (1888) I.L.R. 10 All. 272.
(6) (1899) 26 I.A. 83.
(7) (1918) I.L.R. 41 Mad. 778.
(8) (1944) 12 I.T.R. 489.
(9) (1937) 5 I.T.R. 269.

is to determine whether the allowance would cease if the assessee ceased to be a member of the undivided family: see also *Shrimati Maharani Laxmipat Mahadevi Garu Dowager Maharani of Jeypore* v. *Commissioner of Income-tax, U.P., C.P., and Berar* [1]. If we apply this test to the present case, the answer must necessarily be against the assessee. The assessee is entitled to a definite maintenance allowance under a registered deed and the deed does not say that she will receive this allowance only so long as she is a member of the Hindu undivided family. The law to be applied in the present case cannot, in my opinion, be different from that applied in *Shrimati Maharani Laxmipat Mahadevi Garu Dowager Maharani of Jeypore* v. *Commissioner of Income-tax, U.P., C.P., and Berar* [1], already cited, where the assessee was a lady belonging to the Jeypore family to which the present assessee is said to belong and was much more closely related to the holder of the estate than the assessee. The facts of that case were these. Upon the death of the assessee's husband a dispute arose between her and his successor over the title to the estate and certain house property. The dispute was settled by the execution of a deed of settlement and compromise. Under the deed the assessee acknowledged the absolute title of the Raja in the estate and disclaimed, relinquished and conveyed in favour of the Raja whatever rights she might have had in the properties and the Raja on his part agreed that he and his heirs should pay a sum of one lakh of rupees every year for and on her behalf and the same was to be secured by a charge on the estate. The Raja also agreed to pay her a certain sum for providing her with a suitable residence and for her medical treatment. The assessee claimed that the annual allowance received by her under the deed was exempt from taxation under Section 14 (1) of the Income-tax Act. This claim was, however, negatived.

In the present case it is not at all clear that the assessee has received the allowance as a member of a Hindu undivided family. There is nothing to show that she used to receive any allowance before she executed the deed and there is no statement in the deed that the allowance was to be paid to her as a member of a Hindu undivided family. It is to be observed incidentally that the sum which was fixed as allowance was made the first charge on the Madgole estate and not on the Jeypore estate. If the Maharaja was liable to pay her an allowance apart from the deed and because of her being a member of a Hindu undivided family, the allowance might have been made a charge on the Jeypore estate.

Reference may also be made here to *Vikram Deo Maharajulum Garu Maharajah of Jeypore* v. *Vikram Deo Garu* [2] which is also a case

(1) (1944) 12 I.T.R. 489. (2) (1919) 24 C.W.N. 226.

relating to the Jeypore estate and which is often referred to as the "*Jeypore case*[1]." The head-note of that case runs as follows: "In a suit for maintenance by a brother's son of the late Maharajah of Jeypore out of impartible estate of which the latter was and the present Maharajah is now the holder, the defence assumed that the plaintiff had *prima facie* the right to be maintained but pleaded a special custom taking away such a right. The Courts below being of opinion that the defence had failed to prove the alleged custom decreed the suit." It was held by the Privy Council that in view of the decision in *Raja Rama Rao* v. *Raja of Pittapur*[2], the burden was on the plaintiff to prove a custom entitling him to maintenance and not upon the defendants to prove a custom negativing the ordinary law. Apart from custom and from certain near relationships to the holder the junior members of the family of the zamindars entitled to an impartible zamindari have no right of maintenance out of it, and there is no invariable custom by which any member of the family beyond the first generation from the last holder can claim maintenance as of right.

It is said that the law laid down in this case has been unsettled by certain subsequent decisions of the Privy Council; but such an argument is no longer tenable (see *Commissioner of Income-tax, Punjab* v. *Dewan Bahadur Dewan Krishna Kishore*[3]). However that may be, there can be no doubt that at the time when the assessee entered into an agreement with the Maharaja in 1928 the view expressed in the *Jeypore case*[1] was the prevailing view and upon that view the assessee was not entitled to maintenance apart from custom, from the holder of the Jeypore estate. It may be that for that very reason she chose to secure a maintenance allowance for herself by means of a formal deed of agreement and if she chose to enter into an agreement with the Maharaja which made it incumbent upon him to pay certain allowances to her, apart from her position in the family, it cannot be said that she received those allowances as a member of the Hindu undivided family. Reliance was placed by the learned counsel for the assessee upon the decision of this Court in *Commissioner of Income-tax* v. *Maharani Gyan Manjuri Kuari*[4] and that of the Oudh Chief Court in *Commissioner of Income-tax, C. P. and U. P.* v. *Rani Rudh Kumari*[5]. These cases, in my opinion, can be of no help to the assessee. In the first case it was held that a certain maintenance allowance which the mother of a holder of an impartible estate periodically and regularly received from the estate in the hands of her son is exempt from taxation under Section 14 (1) and in support of this view reference was made to

(1) (1919) 24 C.W.N. 226.
(2) (1918) 45 I.A. 148.
(3) (1941) 9 I.T.R. 695.
(4) (1945) 13 I.T.R. 55; I.L.R. 24 Pat. 159.
(5) (1940) 8 I.T.R. 607.

the following passage which was quoted from Mulla's Hindu Law: "A Hindu is under a legal obligation to maintain his wife, his minor sons, his unmarried daughters, and his aged parents whether he possesses any property or not. The obligation to maintain these relations is personal in character, and arises from the very existence of the relation between the parties." If in the present case the assessee belonged to the category of persons referred to in the passage quoted from Mulla's Hindu Law, the position might have been different, but the pedigrees referred to in the order of the Tribunal shows that she is very remotely related to the Maharaja of Jeypore from whom she receives the maintenance allowance in question. The case of *Rani Rudh Kumari* [1] is also distinguishable precisely on the same ground, because in that case also the assessee was the mother of the holder of the estate.

For these reasons, I would hold that the sum of Rs. 19,800 received by the assessee from the Maharaja of Jeypore is not exempt from income-tax under Section 14 (1) of the Income-tax Act and the answer to the first question should be in the negative.

The assessee must pay Rs. 250 as costs to the Commissioner.

MANOHAR LALL, J.—I agree.

Reference answered in the negative.

[IN THE BOMBAY HIGH COURT.]

CHATURBHUJ VALLABHDAS
v.
COMMISSIONER OF INCOME-TAX.

KANIA, AG. C. J., and CHAGLA, J.

September 18, 1945.

INDIAN INCOME-TAX ACT (XI OF 1922), SEC. 4 (3) (i)—CHARITABLE PURPOSES—'CHARITY', MEANING OF—WILL—DIRECTION TO APPLY INCOME FROM RESIDUARY ESTATE TO SUCH ACTS OF CHARITY AS TRUSTEE DEEMS PROPER—WHETHER INCOME EXEMPT FROM TAX.

The word "charity" if used generally or without qualifications or limitations denotes public charity and falls within the definition of "charitable purpose" in Section 4 (3) of the Income-tax Act.

A will contained a provision to the following effect: "My trustee shall utilise my residuary property for such acts of charity as he deems proper. But if my trustee thinks fit, he can give a one-fourth part of my residuary property to all or one or more than one of my daughters or to the sons of my daughters." The residuary estate consisted of

(1) (1940) 8 I.T.R. 607.

immovable properties and securities. The Income-tax authorities sought to tax the whole income of the residuary estate on the ground that it did not fall under Section 4 (3) (i) of the Income-tax Act :

Held, *that the three-fourths of the income of the residuary estate which was directed by the testator to be utilised for charity was income from property held in trust or other legal obligation wholly for religious or charitable purposes and was therefore exempt from assessment under Section 4 (3) (i).*

Cases referred to :—

All India Spinners' Association *v.* Commissioner of Income-tax [1944] (12 I.T.R. 482 ; A.I.R. 1944 P.C. 88 ; 49 C.W.N. 1 ; 47 Bom. L.R. 233 ; 71 I.A. 159).

Maulana Mohammad Ibrahim Riza Malak *v.* Commissioner of Income-tax, C.P. [1930] (57 I.A. 260 ; 4 I.T.C. 486 ; 32 B.L.R. 1538 ; 59 M.L.J. 905 ; A.I.R. 1930 P.C. 226).

Runchordas *v.* Parvatibai [1899] (I.L.R. 23 Bom. 725).

Trikumdas Damodar *v.* Haridas [1907] (I.L.R. 31 Bom. 583).

Trustees of the Tribune, *In re* [1939] (7 I.T.R. 415 ; 41 Bom. L.R. 1150 ; 182 I.C. 882 ; A.I.R. 1939 P.C. 208 ; 66 I.A. 241 ; I.L.R. 1939 Lah. 475).

Reference under Section 66 (1) of the Indian Income-tax Act (XI of 1922) by the Income-tax Appellate Tribunal : Income-tax Reference No. 8 of 1945.

STATEMENT OF CASE.

"This is a reference under Section 66 (1) of the Indian Income-tax Act, at the instance of the assessee Mr. Chaturbhuj Vallabhdas. He invites us to refer for their Lordships' opinion a question of law arising out of our judgment in this appeal (R. A. A. No. 107-Bombay, 1943-44). The Commissioner of Income-tax, Bombay, Sind and Baluchistan, by his written answer agrees to the reference. The application and the written answer are respectively marked Exhibits A and B in the appended list.

2. The material facts are briefly these. One Gordhandas Khetsey died on February 27, 1935, after making a will dated 30th April 1934. The will was duly admitted to probate. A copy of the will in Gujarati, together with an English translation, is placed on the record in the form of a booklet. It appears that the deceased possessed a large estate, movable and immovable. After making a number of dispositions he declared a trust in respect of his residuary estate in clause 15 of the will which is as follows :—

" *Clause 15.*—My trustee shall utilize my residuary property for such acts of ' charity ' as he deems proper. But if my trustee thinks fit, he can give a one-fourth part of my residuary property to all or one or more than one of my daughters or to the sons of my daughters."

The residuary estate consists of immovable properties in Bombay and its suburbs, as well as securities.

The assessee is the executor and trustee appointed by the will. In his legal character as trustee he has been assessed in respect of income from the trust properties just mentioned. The Income-tax Officer computed the total income at Rs. 53,367 and levied the tax at the maximum rate, rejecting the assessee's contention that the whole of the income was exempt from taxation under Section 4 (3) (i) of the Act by reason of its being income from property held in trust wholly for religious or charitable purposes. In appeal, the Appellate Assistant Commissioner reduced the assessable income to Rs. 47,566 holding that Rs. 5,801 out of the total income was exempted from taxation being in fact utilised for charitable purposes within the meaning of the section. Copies of the Income-tax Officer's and the Appellate Assistant Commissioner's orders are Exhibits C and D.

4. The assessee appealed to the Appellate Tribunal but confined his claim to exemption only in respect of three-fourths of the income, having regard to the provision in clause 15 of the will which gave power to the trustee to part with one-fourth of the residuary estate in favour of the deceased's daughters or their sons. Thus the main question before us was whether the three-fourths of the income from the residuary estate was income from properties held in trust wholly for religious or charitable purposes within the meaning of Section 4 (3) (i) of the Act. It was alternatively contended that at least a part of the residuary estate was held in trust for such purposes, so that the portion of the income was exempt from taxation. On both these points we held against the assessee. Our reasons are stated in paragraphs 4 and 5 of our judgment (Exhibit E). Briefly speaking we held that the term "charity" vaguely described in clause 15 of the will did not necessarily mean a charitable purpose within the meaning of Section 4 (3) (i) of the Act, and that the trustee was at liberty to utilise the whole of the income for any charity, public or private, just as he liked. We also held that the residuary estate was not held in part for religious or charitable purposes so as to entitle the assessee to claim a partial exemption in respect of income so applied. It was contended that the trustee was applying the income towards charitable purposes but our view was that the application of the income was not material and what was necessary was that the property must be held in trust.

5. The assessee also took exception to the tax being levied at the maximum rate. But that point has not been taken in the reference which asks us to refer only one question.

6. Accordingly we submit the following question for their Lordships' opinion :—

Question referred—Whether in the circumstances of the case and on a true construction of clause 15 of the will of late Gordhandas Khetsey the income from the deceased's residuary estate is income from property held in trust or other legal obligation wholly for religious or charitable purposes so as to be exempt from assessment under Section 4 (3) (i) of the Act ?"

Sir J. B. Kanga and *R. J. Kolah,* for the assessee.

M. C. Setalvad, for the Commissioner.

JUDGMENT.

KANIA, AG. C. J.—This is a reference under Section 66 (1) of the Income-tax Act by the Tribunal of Income-tax, inviting the Court's opinion on the following question :—

"Whether in the circumstances of the case and on a true construction of clause 15 of the will of late Gordhandas Khetsey the income from the deceased's residuary estate is income from property held in trust or other legal obligation wholly for religious or charitable purposes so as to be exempt from assessment under Section 4 (3) (i) of the Act ?"

The material facts are few. Gordhandas Khetsey made his will dated 30th April 1934 and died on 27th February 1935. He left a large estate. Clause 15 of the will runs as follows :—

"My trustee shall utilize my residuary property for such acts of charity as he deems proper. But if my trustee thinks fit, he can give a one-fourth part of my residuary property to all or one or more than one of my daughters or to the sons of my daughters."

In the statement of case it is stated that the residuary estate consists of immovable properties in Bombay and its suburbs and also securities. The taxing authorities sought to tax the whole income of the residue on the ground that it did not fall under Section 4 (3) (i) of the Income-tax Act. Before the Assistant Commissioner it was in fact found that a certain amount was spent for religious and charitable purposes and he permitted the amount to be exempted from tax. Except for that, he directed that the balance should be taxed at the maximum rate. The assessee appealed. The Commissioner did not appeal against the order of the Assistant Commissioner. Before the Tribunal it was argued that the word "charity" used in clause 15 of the will was not covered by the definition of "charitable purpose" found at the end of Section 4 of the Act. That definition runs as follows :—

"In this sub-section 'charitable purpose' includes relief of the poor, education, medical relief, and the advancement of any other object of general public utility."

It was contended on behalf of the Commissioner that the word "charity" was indefinite and may include public or private charity, and also benevolent or philanthropic objects. Therefore, the income of the residue was not exempt from taxation under the Act. This line of reasoning is found in the judgment of the Tribunal. The assessee asked the above-mentioned question of law to be referred to the Court and the matter has thus come before us.

In my opinion the meaning put on the word "charity" (used in clause 15 of the will) in the judgment of the Tribunal is incorrect. "Charity" without any further qualifications has a recognised meaning in law. It amounts to a general charitable intention for objects well recognised as charitable in law. It is to be noticed in this case that the original will is in Gujarati but the testator has deliberately used the word "charity" (an English word) in writing out clause 15. This may be due to the fact that the Gujarati word "*Dharam*" has been held to be void for uncertainty. We are not concerned in this case with what the Gujarati equivalent may be, or what effect can be given if a Gujarati word was used. Taking the word "charity" as used in clause 15 I see no justification for the conclusion of the Tribunal that it would include benevolent or philanthropic objects or it may be private charity. The expression "private charity," strictly speaking, is a misnomer. The words "charity" or "charitable purpose" or "charitable object" are defined in various sections of different Acts of the Indian legislature. In all of them the idea of public benefit is clearly involved.

It was sought to be argued on behalf of the Commissioner that in the present case by the use of the word "charity" without the word "public" the use for public was not necessarily indicated. In this connection Mr. Setalvad relied on the judgment of the Privy Council in *All India Spinners' Association* v. *Commissioner of Income-tax*[1]. In that case the Court was considering whether the objects of the Association were charitable or not. It must be noted that the word "charity" was not used as one of the objects of the Association. Their Lordships emphasized that in the definition given in the Income-tax Act the word "public" was used and it was of importance. From that observation it was sought to be argued on behalf of the Commissioner that unless the word "public" was used in connection with the objects mentioned in the settlement, the same was not within the meaning of "charitable purpose" as defined in the Act. In my opinion, that argument is unsound. Their Lordships were only considering the particular objects of the Association before them, and in considering the different objects emphasized

(1) (1944) 12 I.T.R. 482.

the view that if the use was for the benefit of the public, or a section of the public it was an important factor to be considered in determining whether the object was charitable or not. In my opinion, it is misreading that case to say that when in a settlement the word "charity" is used without any qualifications or limitations it is not covered by the definition found in the Income-tax Act, unless the word "public" is expressly used in connection with "charity." I would put the position in a different way. The word "charity," if used generally, necessarily connotes the use for the public. Therefore, when the word "charity" is used, there is nothing to include in it objects of private benefit only. In my opinion, the word "charity," if used generally or without qualifications or limitations, falls within the definition of "charitable purpose" found in Section 4 of the Act.

One of the tests to be applied is whether the gift in question is valid in law. This argument was supported by the observations of the Privy Council in *Trustees of the Tribune, In re*[1]. In the course of the judgment it was observed as follows :—

"Their Lordships are in agreement with this view and see nothing in the Indian Income-tax Act to discharge the Court of its responsibility in coming to a finding as to the character of the object of a trust—a matter which bears directly upon its validity."

Therefore if a gift to charity is held valid according to the laws of India, it is a relevant factor to be considered in deciding if it is a charitable purpose within the meaning of the Act. *Runchordas Vandravandas* v. *Parvatibai*[2], and *Tricumdas Damodar* v. *Haridas Morarji*[3], show that the word "charity," used generally, gives rise to a good bequest or gift in India. In my opinion, therefore, the construction put upon that word in clause 15 of the will by the Tribunal is not correct. The word "charity" used generally and without limitations by itself is sufficient to fall within the definition of charitable purpose given in the Indian Income-tax Act and the argument of the Commissioner on this point must be rejected.

It was next argued that in the present case by clause 15 no specific property is set apart for charity and therefore the case is covered by the second part of Section 4 (3) (i) which runs in these terms :—

"4. (3) This Act shall not apply to the following classes of income :—

(i) Any income derived from property held under trust or other legal obligation wholly for religious or charitable purposes, and in the case of property so held in part only for such purposes, the income applied, or finally set apart for application, thereto."

(1) (1939) 7 I.T.R. 415, at p. 422.
(2) (1899) I.L.R. 23 Bom. 725.
(3) (1907) I.L.R. 31 Bom. 583.

It was argued that in the present case the residuary estate was not property held in trust or for other legal obligation " wholly " for religious or charitable purpose. At most therefore only such portion of the income as is proved to be applied for such purposes should be exempted from tax. Mr. Setalvad relied on the judgment of the Privy Council in *Maulana Mohammad Ibrahim Riza Malak* v. *Commissioner of Income-tax*[1]. In that case a property was settled on trust under a deed dated 25th August 1917. The objects of the trust were further explained and extended by another deed dated 25th November 1922. An examination of the documents showed clearly that the income of the trust property was applicable to purposes many of which were neither religious nor charitable. On the construction of the documents their Lordships held that the income of the property so settled was not held in trust wholly for religious or charitable purposes. There can be no doubt on that point. Their Lordships then observed as follows:—" Nor is it suggested that any part of the property is set aside for any charitable or religious purposes, so that it can be identified as appropriated exclusively to such purposes." Relying on that observation and the statement in the case here that the residuary estate consists of immovable properties in Bombay and its suburbs as well as securities, it was argued that the assessee cannot point out any particular property which was set apart exclusively for charitable purposes, and therefore the case was not covered by the first part of Section 4 (3) (i) of the Act. In my opinion this argument is unsound. What their Lordships of the Privy Council were concerned with was a case in which several objects were mentioned in a deed to which income could be applied. It was not stated in the deed what portion of the income was to be applied for the purpose set out in a particular clause. The result was that the trustees could use any portion of the income or the whole income for either charitable or non-charitable purposes. In such circumstances it was obvious that the Board had to hold that exemption could be granted only in respect of what was actually used for charitable purposes. The observation quoted above has to be read in the light of those facts. Their Lordships had under those circumstances to state that as it could not be identified that any part of the property was appropriated exclusively to charitable purposes the first part of clause (i) of sub-section (3) could not be applicable. I am unable to read that observation as meaning that the trustees must point out a particular property (*i.e.*, a house, or a security giving the number) to bring into operation the first part of the clause. Residuary estate is recognised as property in law. If so, a clearly

(1) (1930) 4 I.T.C. 486; 57 I.A. 260.

defined portion of the residuary estate is equally "property" within the meaning of law. In the present case by clause 15 the testator had directed his trustee to utilise three-fourths of the income of the residuary estate for charity. That clearly falls within the first part of clause (i) of sub-section (3) of Section 4 of the Act. As regards the remaining one-fourth part the trustee is given the option to spend it either for charity or to give the same over to one or more of the testator's daughters or the sons of his daughter. To that part the second portion of clause (i) may be applied. We are not concerned with that point as it is agreed between the parties that the question before the Court should be limited only to three-fourths of the income of the residue. In my opinion that income is clearly covered by Section 4 (3) (i), first part. That portion of the residue is held wholly for charitable purposes within the meaning of the Income-tax Act, and is completely exempt from tax.

Our answer to the question submitted for the Court's opinion (limited to the three-fourths of the income of the residuary estate) is in the affirmative. The Commissioner to pay the costs of the reference.

CHAGLA, J.—I agree. In my opinion when an assessee claims exemption under Section 4 (3) (i) on the ground that the income is derived from property held under trust or other legal obligation wholly for religious or other charitable purposes the responsibility is cast upon the Court to determine and decide whether such a trust is a valid one. In the case of *Trustees of the Tribune, In re*[1], the trustees of the Tribune claimed exemption under sub-section (3) of Section 4 on the ground that the income was spent for the advancement of an object of general public utility and their Lordships of the Privy Council there pointed out that it was the duty of the Court to determine what the character of the object was; whether in the opinion of the Court the object was such as would advance public utility. In the case before us the testator has not indicated the object of the charity. All that he has stated is that the trustees should spend the income of his residue for such acts of charity as he deemed proper. Now, in my opinion, considering the fact that this is the will of a Gujarati speaking person writing in the Gujarati language, it is clear that the intention of the testator, by using the word "charity" which is an English expression, was to indicate and disclose a dominant and overriding charitable intention which was not the case before the Privy Council, to which I have referred. Their Lordships cast a duty upon the Court to determine whether the printing of the paper was for the purpose of public advancement. Similarly it is our duty to determine whether the bequest contained in clause 15 is a valid charitable bequest. It is clear on the

(1) (1939) 7 I. T. R. 415.

authorities, and I need not refer to them, that if a dominant charitable intention is disclosed although the object of the charity is not indicated the Court will not permit the charitable bequest to be defeated but if necessary may administer the trust and undertake the control of the trust. Therefore in my opinion this is a good charitable bequest, and if it is a good charitable bequest, it falls within the terms of Section 4 (3) (i) and is a trust for charitable purposes. I therefore agree that the answer to the question referred to the Court should be in the affirmative and the Commissioner should pay the costs of the reference. *Reference answered in the affirmative.*

[IN THE LAHORE HIGH COURT.]

COMMISSIONER OF INCOME-TAX, PUNJAB

v.

SARAN SINGH RAM SINGH.

DIN MOHAMMAD, SALE, MUHAMMAD MUNIR, MEHR CHAND MAHAJAN and KHOSLA, JJ.

December 17, 1945.

INDIAN INCOME-TAX ACT (XI OF 1922), SECS. 25 (4), 25A, 26—HINDU UNDIVIDED FAMILY—PARTITION—BUSINESS TAXED UNDER 1918 ACT ALLOTTED TO MEMBER—WHETHER FAMILY ENTITLED TO RELIEF UNDER SECTION 25 (4)—SCOPE OF SECS. 25 (4), 25A, 26.

Where a Hindu undivided family carrying on a business which was taxed under the Indian Income-tax Act, 1918, partitioned the family properties and allotted the business to one of its members who thereafter carried it on :

Held, *that there was a succession, and although an assessment should be made on the members of the family under Section 25A (2), the family was entitled to the relief under Section 25 (4).*

There is no inconsistency, repugnancy or conflict between the provisions of Sections 25 (4), 25A (2) and 26 (2) of the Act. Each deals with a different set of circumstances.

Notwithstanding the partition, the family, by virtue of Section 25A, must be regarded as joint for the purposes of assessment which must include the grant of relief under Section 25 (4).

Kotha Govindarajulu Chettiar v. *Commissioner of Income-tax, Madras* [1944] (12 I.T.R. 97 ; I.L.R. 1944 Mad. 504) *followed.*

Cases referred to :—

Kotha Govindarajulu Chettiar *v.* Commissioner of Income-tax, Madras [1944] (12 I.T.R. 97 ; I.L.R. 1944 Mad. 504).

Ram Rakha Mal and Sons Ltd. *v.* Commissioner of Income-tax, Punjab [1937] (5 I.T.R. 137; 18 Lah. 325; 39 P.L.R. 934 ; A.I.R. 1937 Lah. 830).

Sir Sundar Singh Majithia *v.* Commissioner of Income-tax [1942] (10 I.T.R. 457 ; 202 I.C. 483 ; A.I.R. 1942 P.C. 57 ; I.L.R. 1943 All. 69).

Case referred by the Income-tax Appellate Tribunal, Allahabad, under Section 66 (1) of the Indian Income-tax Act, 1922: (Civil Reference Case No. 17 of 1943).

STATEMENT OF CASE.

"This is an application under Section 66 (1) of the Income-tax Act made by the Commissioner of Income-tax, Punjab and N. W. F. Provinces, requiring us to refer to the High Court of Judicature at Lahore, two questions of law, said to arise out of the order under Section 33, dated 16th September 1942, of this Bench of the Tribunal, as it was then constituted, in R.A.A. No. 131-(Punjab) of 1941-42, relating to the respondent's assessment for 1941-42.

2. A Hindu undivided family consisted of S. Pratap Singh and his two sons, S. Bahadur Singh and S. Lachman Singh. The assessment for 1941-42 was made on the income of the accounting period from 8th April 1940 to 25th March 1941. The Income-tax Officer, A. Ward, Amritsar, passed an order under Section 25-A (1), whereby he held that a partition had taken place amongst the members of the old Hindu undivided family with effect from 25th March 1941. The assessment was made under Section 23 (3) read with Section 25-A (2). The old Hindu undivided family that was assessed as if no partition had taken place had applied to the Income-tax Officer for the relief provided for under Section 25 (3). The Income-tax Officer held that there was no discontinuance and so Section 25 (3) did not apply, inasmuch as "the discontinuance contemplated by Section 25 (3) is a total discontinuance of business and not its splitting up as in the present case." It was then urged before him that the claim of the Hindu undivided family might be considered under sub-section (4) of Section 25. The Income-tax Officer's conclusion in regard to this additional or alternative claim was that when assessment is to be made under the provisions of Section 25-A (2), even when there is succession, the provisions of Section 25 (4) should not apply. He further held that the business styled Saran Singh Ram Singh "has not been discontinued but has been split up. In such cases where business has been split up, it has been held that there is no succession." His final order therefore was that in the case before him the relief contemplated by Section 25 (3) or 25 (4) was not available to the old Hindu undivided family.

3. The matter then went up to the Appellate Assistant Commissioner, Amritsar, who affirmed the Income-tax Officer's finding that there was neither discontinuance nor succession in this case, so that the relief claimed by the assessee family was not allowable.

4. The respondent then preferred a second appeal to the Tribunal, which held that the conclusion of the Income-tax authorities that there was no discontinuance in the present case was correct, but that there was succession so that the assessee was entitled to the relief contemplated in Section 25 (4) of the Act.

5. The respondent had several businesses and house properties. It is common ground that the claim in regard to relief under Section 25 (3) was preferred only in respect of the *kariana* and yarn business carried on by the old Hindu undivided family at Amritsar—this was the only business, the income of which was charged to income-tax under the Income-tax Act of 1918. By mutual consent this *kariana* and yarn business was given over to S. Bahadur Singh as the result of a partition of the joint family assets. In order, however, to equalise the share of his brother (S. Lachman Singh) in the assets of the family, a portion of the stock of this business was given over to S. Lachman Singh; the stock at the time of partition amounted to Rs. 2,66,618, out of which, stock worth Rs. 1,01,851 was made over to S. Lachman Singh; a few of the import contracts with foreign shippers appertaining to this business also fell to the share of S. Lachman Singh. On these facts the Bench of the Tribunal, for reasons mentioned in its order under Section 33, held that S. Bahadur Singh succeeded to the old Hindu undivided family's *kariana* and yarn business, because "in this case the present business is being carried on at the old premises under the same name and style, the successor having taken charge of all outstandings of the old business, which can clearly be identified with the business that is now being carried on by S. Bahadur Singh."

6. In paragraph 4 of the application for reference, the applicant states that some of the assets and liabilities had also fallen to the share of S. Lachman Singh on partition, in addition to what stocks and import contracts have been referred to in the order under Section 33 (and mentioned above in the preceding paragraph). This point was not raised before the Bench at the time of the hearing of the appeal, and it will also appear from the order of the Appellate Assistant Commissioner under Section 31 that he too did not mention the division of such assets and liabilities of the *kariana* and yarn business between the two brothers. At the hearing of the application for reference before us, Mr. Kirpa Ram Bajaj, Advocate, who appeared on behalf of the respondent, stated that the assets worth Rs. 2,930, mentioned in the application for reference, did not appertain to the *kariana* and yarn business and that the liabilities to the extent of Rs. 30,473, mentioned in the application for reference as having been taken over by S. Lachman Singh, consisted of liabilities of the old Hindu undivided

family to S. Lachman Singh himself and to his wife and daughters and to some others, which had nothing to do with the *kariana* and yarn business. These are, however, facts, which cannot be verified at this late stage; suffice it to say that even if assets worth Rs. 2,930 and liabilities to the extent of Rs. 30,473, taken over by S. Lachman Singh are taken for the sake of argument to appertain to the *kariana* and yarn business, having regard to the fact that assets and liabilities of the business worth Rs. 1,85,327 and Rs. 2,57,749 respectively fell to the share of S. Bahadur Singh, the Bench would have had no hesitation to say that this so called division made little or no difference, so far as its conclusion as to succession was concerned—the Bench did not consider the making over of a substantial portion of the stock of the business to S. Lachman Singh (in order to equalise his share in the family assets with that of his brother) as standing in the way of its holding that there was succession in this case.

7. On these facts the applicant asks us to refer to the High Court the following two questions:

" Whether in the case of succession to a business formerly carried on by a Hindu undivided family, assessment is to be made under Section 26 (2) read with Section 25 (4) or under Section 25-A (2)," and "whether in the circumstances of this case there was no succession within the meaning of Section 26 (2) and Section 25 (4) but only a splitting up of the business."

8. In the reply of the respondent to the application for reference, under Rule 54 of the Appellate Tribunal Rules, it is stated " that in view of the clear finding of succession, which is essentially a question of fact, no question of law arises." It has also been urged in the reply " that Section 25-A (2) has no application. Even if it be held applicable, Section 25 (4) and Section 25-A (2) will still govern the case."

9. We, however, think that a question of law certainly does arise in this case. Both the questions framed by the applicant proceed on the assumption that Section 25 (4) is " applicable to successions under Section 26 (2), but not to those under Section 25-A (2)." This point was brought out by the Income-tax Officer in his order on the respondent's application to him for relief under Section 25 (3) or Section 25 (4). It may, however, be mentioned here that this point, stressed by the Income-tax Officer, was not discussed by the Appellate Assistant Commissioner in appeal, nor was it canvassed before the Bench of the Tribunal at the hearing of the second appeal. But we do not wish to brush aside the point on any technical or superficial ground; the point does involve a question of law; it was raised at some previous stage; the facts are also all known. At the same time the questions, as framed

by the applicant, do not appear to us to be suitable for referenc particularly because the applicant has laid the main stress on Sectic 26 (2), which the Bench of the Tribunal had no occasion to discus The point or points on which the applicant desires a decision of the Lordships can, however, be understood from the questions drafted b him. These points may be incorporated in questions framed differen ly in the light of the Tribunal's order under Section 33. In our vie the referable questions of law may be framed as below :—

"(1) Whether, in the circumstances of the case, there was succes sion by S. Bahadur Singh to the *kariana* and yarn business, or th business was split up between S. Bahadur Singh and S. Lachma Singh so as to constitute discontinuance of the old business."

"(2) Whether, on the facts of the case, the application of Sectio 25-A (2) is a bar to the assessee's claim either under Section 25 (4) o Section 25 (3)."

10. Both the learned Departmental Representative and the learne Advocate and the learned Accountant, who represented the respondent agreed to this form of the questions. In the circumstances, we refer th following two questions for the decision of the Hon'ble High Court :—

"(1) Whether, in the circumstances of the case, there was succes sion by S. Bahadur Singh to the *kariana* and yarn business, or the business was split up between S. Bahadur Singh and S. Lachman Singh so as to constitute discontinuance of the old business."

"(2) Whether, on the facts of the case, the application of Section 25-A (2) is a bar to the assessee's claim either under Section 25 (4) or Section 25 (3)."

[This case was referred by the Division Bench (consisting of Mr. Justice Din Mohammad and Mr. Justice Sale) to a Full Bench by their order dated the 14th April 1944 and the Full Bench (consisting of Sir Trevor Harries, Chief Justice, Mr. Justice Din Mohammad and Mr. Justice Sale) referred the case to the Bench of five Judges by their order dated the 22nd February, 1945.]

Raj Krishna, for the Commissioner.

Kirpa Ram Bajaj and *Narindar Nath Chopra*, for the assessee.

The Order of the Division Bench dated 14th April 1944 was as follows :—

DIN MOHAMMAD and SALE, JJ.—This is a case stated by the Income-tax Appellate Tribunal on the application of the Commissioner of Income-tax.

The relevant facts are these. The assessee, a Hindu undivided family, known as Saran Singh Ram Singh, carried on the business of guarantee brokers to the Central Bank of India Ltd., as well as that of

Indian drugs and yarn at Amritsar and the business of flea seed husk at Sidhpur in Baroda State. The business of Indian drugs and yarn existed prior to 1918 while the other two businesses were started subsequently. On the 17th April, 1941, when the family was composed of Sardar Partap Singh and his two sons, S. Lachman Singh and S. Bahadur Singh, a deed of partition of the joint family business was executed by the persons concerned by which the business of guarantee brokers was allotted to S. Partap Singh, that of flea seed husk to S. Lachman Singh and that of Indian drugs and yarn to S. Bahadur Singh. It was stated in the deed that the family had actually disrupted on the 25th March, 1941, and divided all the immovable and movable property along with business assets, furniture etc., on that date. Consequent upon this, S. Partap Singh submitted an application to the Income-tax Officer claiming an order under Section 25-A of the Act and this was made on the 31st July, 1941. Simultaneously, in respect of the Indian drugs and yarn business at Amritsar, he put in another application under sub-section (3) of Section 25, which deals with discontinuance of any business, profession or vocation on which tax was at any time charged under the provisions of the Indian Income-tax Act, 1918. In the course of arguments before the Income-tax Officer, however, he relied on sub-section (4) of Section 25 as well, which deals with succession to such business. The Income-tax Officer, on the same date, repelled this contention holding that neither sub-section (3) nor sub-section (4) could be invoked.

Against this decision, the assessee took an appeal to the Appellate Assistant Commissioner, which was rejected on the 10th December, 1941. The assessee then preferred an appeal to the Income-tax Appellate Tribunal and the Bench before whom the appeal came on for hearing allowed the appeal holding that the assessee was entitled to the benefit of sub-section (4) of Section 25. Being dissatisfied with this decision, the Commissioner of Income-tax moved the Tribunal with the result as stated above.

It is contended on behalf of the Commissioner that, in the first place in view of clauses (4) and (9) of the deed, S. Bahadur Singh was to run a business of his own and not the old business in the old style, although he was allowed to retain its name, and secondly, even if it were a case of succession, the case fell under the specific provisions of sub-section (2) of Section 25-A, inasmuch as the business succeeded to was formerly carried on by a Hindu undivided family. The assessee, on the other hand, refers to a decision of a Bench of this Court, of which I was a member, reported in *Ram Rakha Mal and Sons Ltd.* v. *Commissioner of Income-tax, Punjab* [1] as well as to a judgment of five

(1) (1937) 5 I.T.R. 137; I.L.R. 18 Lah. 325.

Judges of the Madras High Court reported as *Kotha Govindarajulu Chettiar* v. *Commissioner of Income-tax, Madras* [1], and urges that he is clearly entitled to the benefit of sub-section (4) of Section 25. It may be observed that the assessee no longer relies on sub-section (3) of that section, conceding frankly that the business had not discontinued as contemplated by that sub-section.

I may say at once that the first contention raised by the Commissioner is devoid of force. There is no question but that S. Bahadur Singh was to continue the old business as it stood at the material time, and although the existing contract relating to flea seed and flea seed husk was to be carried out by S. Lachman Singh, it did not in any way convert S. Bahadur Singh's business into a new business of his own. The second question raised by the Commissioner, however, deserves full consideration.

Before the Income-tax Act was amended in 1939, Section 25 dealt with assessment in the case of a discontinued business, profession or vocation and consisted of four sub-sections. Sub-sections (1) and (2) dealt with a business, profession or vocation on which income-tax was *not* at any time charged under the provisions of the Indian Income-tax Act, 1918; sub-section (3) dealt with a business, profession or vocation on which tax *was* so charged, and sub-section (4) laid down the procedure to be followed when making an assessment under sub-section (1) or sub-section (3). Section 25-A dealt with assessment after partition of a Hindu undivided family. Sub-section (1) of this section provided for the disposal of a claim made by any member of a Hindu undivided family that a partition has taken place and sub-section (2) enacted that when such a claim was admitted, the Income-tax Officer was bound to make an assessment as if no separation or partition had taken place and hold each member or group of members liable for a share of the tax on the income so assessed. Sub-section (3) laid down the consequences which would follow in case the claim was rejected. Sub-section (1) of Section 26 dealt with a change in the constitution of a firm and sub-section (2) of the same section provided for a succession to a business, profession or vocation at any time before assessment was made.

After the amendment introduced in 1939, however, Section 25 was expanded into six sub-sections. Sub-sections (1) and (2) of that section were left in tact. Sub-section (3) was amended and the words " then, unless there has been a succession by virtue of which the provisions of sub-section (4) have been rendered applicable," were added. Old sub-section (4), with consequential amendment, was inserted as sub-section (6) and two new sub-sections were added in the shape of sub-sections

(1) (1944) 12 I.T.R. 97.

(4) and (5). By the new sub-section (4) it was enacted that where the person who was at the commencement of the Indian Income-tax (Amendment) Act, 1939 (VII of 1939), carrying on any business, profession or vocation on which tax was at any time charged under the provisions of the Indian Income-tax Act, 1918 (VII of 1918), was succeeded in such capacity by another person, the change not being merely a change in the constitution of a partnership, no tax would be payable by the first mentioned person in respect of the income, profits and gains of the period between the end of the previous year and the date of such succession, and such person could further claim that the income, profits and gains of the previous year should be deemed to have been the income, profits and gains of the said period. It was further provided that where any such claim was made, an assessment would be made on the basis of the income, profits and gains of the said period, and, if an amount of tax had already been paid in respect of the income, profits and gains of the previous year exceeding the amount payable on the basis of such assessment, a refund would be given of the difference. The new sub-section (5) prescribed the period of limitation for claiming the relief afforded under sub-section (3) or sub-section (4).

Section 25-A was also amended. In sub-section (1) of this section the words "that a separation of the members of the family has taken place" were deleted and in sub-section (2) thereof the following words were added :—

"or where any person has succeeded to a business, profession or vocation formerly carried on by a Hindu undivided family whose joint family property has been partitioned on or after the last day on which it carried on such business, profession or vocation."

Both sub-sections (1) and (2) of Section 26 were also materially altered and in sub-section (2) it was provided that where a person carrying on any business, profession or vocation had been succeeded in such capacity by another person, such person and such other person would, subject to the provisions of sub-section (4) of Section 25, each be assessed in respect of his actual share, if any, of the income, profits and gains of the previous year.

It is obvious that although originally succession was dealt with in Section 26 alone, after the amendment, the succession to a business carried on by a Hindu undivided family was specifically provided for in sub-section (2) of Section 25-A, irrespective of the fact whether such business was at any time charged under the provisions of the Indian Income-tax Act, 1918, or not. The question naturally arises why in the face of this provision, the succession to a business, carried

on by a Hindu undivided family which was charged under the Indian Income-tax Act, 1918, should in spite of this amendment be governed by sub-section (4) of Section 25 which deals generally with such business.

No assistance for the solution of this problem can be sought from *Ram Rakha Mal and Sons Ltd.* v. *Commissioner of Income-tax, Punjab*[1], for the simple reason that that decision was given under the old Act and not the amended Act. The Madras case, however, is relevant and fully supports the contention raised on behalf of the assessee. It is unfortunate, however, that in the judgment delivered by Sir Lionel Leach, Chief Justice, on behalf of the Bench, there is no discussion of the new provisions made in sub-section (2) of Section 25-A, and no reasons recorded as to why in the presence of this specific provision, recourse should be had to the general provision as contained in sub-section (4) of Section 25.

As I look at the matter, the specific provision made in sub-section (2) of Section 25-A should, in accordance with the fundamental canon of the interpretation of statutes, override the general provisions made in sub-section (4) of Section 25, and consequently whether a business carried on by a Hindu undivided family was at any time charged under the provisions of the Indian Income-tax Act, 1918, or not, the succession to it should be governed by sub-section (2) of Section 25-A. Counsel for the assessee, however, argues that in these circumstances, a Hindu undivided family would be deprived of the benefit provided for in sub-section (4) of Section 25 as well as that of sub-section (2) of Section 26 and this according to him the legislature could not intend. No doubt the consequence envisaged by counsel would follow if this procedure is adopted, but sitting as a Court of law our function is merely to administer the law as it is, and not to be influenced by the consideration whether the result is equitable or otherwise. We cannot ignore that the words newly inserted in sub-section (2) unequivocally contemplate the succession of any person to a business, profession or vocation formely carried on by a Hindu undivided family whose joint family property has been partitioned on or after the last day on which it carried on such business, profession or vocation, and that there is no qualification or reservation attached to them nor can we introduce in these words any qualification or reservation that may tend to bring this provision into consonance with sub-section (4) of Section 25. Left to myself, therefore, I would agree with the Commissioner that in the case of a Hindu undivided family it is sub-section (2) of Section 25-A that is to be applied and not sub-section (4) of Section 25, but as there is a judgment of five Judges of the Madras High Court in

(1) (1937) 5 I.T.R. 137; I.L.R. 18 Lah. 325.

favour of the contrary view, I would forward this case to the Hon'ble Chief Justice with a recommendation that a larger Bench may be constituted to dispose of the matter in controversy.

SALE, J.—I agree with the recommendation proposed.

The order of the Full Bench dated 22nd February 1945 was as follows :—

HARRIES, C. J., DIN MOHAMMAD and SALE, JJ.—On further consideration, we are of opinion that this case be heard by a Bench of five Judges and we direct accordingly.

S. M. Sikri and *Jindra Lal*, for the Commissioner.

Kirpa Ram Bajaj and *Narindra Nath Chopra*, for the assessee.

JUDGMENT.

MUHAMMAD MUNIR, J.—This is a case stated by the Appellate Tribunal under sub-section (1) of Section 66 of the Indian Income-tax Act. The question to which an answer has to be returned is:

"Whether, on the facts of the case, the application of Section 25-A (2) is a bar to the assessee's claim either under Section 25 (4) or Section 25 (3)?"

The question came to be referred in the following circumstances :—

The assessee was a Hindu undivided family consisting of three members, namely, Partap Singh and his sons Lachman Singh and Bahadur Singh. The family carried on business of guarantee brokers to the Central Bank of India Ltd., and of grocery and yarn at Amritsar and of flea seed husk at Sidhpur in the Baroda State. Up to the year of assessment 1940-41 the family was assessed as undivided but in the course of the assessment for the year 1941-42 the family submitted an application under Section 25-A of the Act and claimed that a partition had taken place among the members of the family and all the joint property divided between the father and the sons on 25th March, 1941. The deed of partition is dated 17th April, 1941, but it refers to the date of partition as 25th March, 1941. According to the deed of partition, the business of guarantee brokers was allotted to Sardar Partap Singh, that of flea seed husk to Sardar Lachman Singh and that of grocery and yarn to Sardar Bahadur Singh. Of these businesses, that of grocery and yarn which fell to the share of Sardar Bahadur Singh was an old business on which tax had been charged under the Indian Income-tax Act, 1918. The Income-tax Officer after the necessary enquiry recorded an order under sub-section (1) of Section 25-A recognising that the family had partitioned its property on 25th March, 1941, and made assessment on the members of the family under sub-section (2) of Section 25-A. The family claimed that since the business

of grocery and yarn had been assessed to income-tax under the Act of 1918, it was, under sub-section (3) of Section 25 of the Act, not liable to pay any tax on the income from 18th April, 1940, to 25th March, 1941, *i. e.*, from the date of commencement of the previous year to the date of discontinuance of the business. The Income-tax Officer rejected the claim, holding that the business had neither been discontinued within the meaning of sub-section (3) nor succeeded within the meaning of sub-section (4) of Section 25 and that, therefore, the family was not entitled to the relief claimed. From this order, an appeal was taken to the Assistant Commissioner who agreed with the Income-tax Officer and dismissed the appeal. Thereupon the family appealed to the Appellate Tribunal which by its order dated 16th September, 1942, allowed the appeal and held that there had been a succession to the grocery and yarn business within the meaning of sub-section (4) of Section 25 of the Act and that the family was entitled to the benefit of that sub-section. The Commissioner of Income-tax being dissatisfied with this order required the Appellate Tribunal to state the case to the High Court. In compliance with this application the Tribunal stated the case and referred to this Court the following two questions :—

(1) Whether, in the circumstances of the case, there was succession by Sardar Bahadur Singh to the *kariana* and yarn business, or the business was split up between Sardar Bahadur Singh and Sardar Lachman Singh so as to constitute discontinuance of the old business?

(2) Whether, on the facts of the case, the application of Section 25-A (2) is a bar to the assessee's claim either under Section 25 (4) or Section 25 (3)?

The reference came up before my brothers Din Mohammad and Sale who by their order dated 14th April, 1944, held that there had been a succession to the grocery and yarn business within the meaning of sub-section (4) of Section 25 and sub-section (2) of Section 25-A; but in view of the novelty and importance of the point involved in the second question they referred the case to a Full Bench.

The contention of the learned counsel for the Commissioner is that since the Hindu undivided family did not exist at the time of the assessment no relief under sub-section (4) of Section 25 could be granted and that in any case since sub-section (2) of Section 25-A is applicable to the case, sub-section (4) of Section 25 ceases to apply. In order to appreciate this contention it is necessary to refer to the relevant provisions of Sections 25, 25-A and 26 of the Act which are as follows :—

"25. (1) Where any business, profession or vocation to which sub-section (3) is not applicable is discontinued in any year, an assessment may be made in that year on the basis of the income, profits or gains of the period between the end of the previous year and the date

of such discontinuance in addition to the assessment, if any, made on the basis of the income, profits or gains of the previous year.

(3) Where any business, profession or vocation on which tax was at any time charged under the provisions of the Indian Income-tax Act, 1918, is discontinued, then, unless there has been a succession by virtue of which the provisions of sub-section (4) have been rendered applicable, no tax shall be payable in respect of the income, profits and gains of the period between the end of the previous year and the date of such discontinuance, and the assessee may further claim that the income, profits and gains of the previous year shall be deemed to have been the income, profits and gains of the said period. Where any such claim is made, an assessment shall be made on the basis of the income, profits and gains of the said period, and, if an amount of tax has already been paid in respect of the income, profits and gains of the previous year exceeding the amount payable on the basis of such assessment, a refund shall be given of the difference.

(4) Where the person who was at the commencement of the Indian Income-tax (Amendment) Act, 1939, carrying on any business, profession or vocation on which tax was at any time charged under the provisions of the Indian Income-tax Act, 1918, is succeeded in such capacity by another person, the change not being merely a change in the constitution of a partnership, no tax shall be payable by the first mentioned person in respect of the income, profits and gains of the period between the end of the previous year and the date of such succession, and such person may further claim that the income, profits and gains of the previous year shall be deemed to have been the income, profits and gains of the said period. Where any such claim is made, an assessment shall be made on the basis of the income, profits and gains of the said period, and, if an amount of tax has already been paid in respect of the income, profits and gains of the previous year exceeding the amount payable on the basis of such assessment, a refund shall be given of the difference.

(6) Where an assessment is to be made under sub-section (1), sub-section (3), or sub-section (4), the Income-tax Officer may serve on the person whose income, profits and gains are to be assessed, or, in the case of a firm, on any person who was a member of such firm at the time of its discontinuance, or, in the case of a company, on the principal officer thereof, a notice containing all or any of the requirements which may be included in a notice under sub-section (2) of Section 22, and the provisions of this Act shall, so far as may be, apply accordingly as if the notice were a notice issued under that sub-section.

25-A. (1) Where, at the time of making an assessment under Section 23, it is claimed by or on behalf of any member of a Hindu family hitherto assessed as undivided that a partition has taken place among the members of such family, the Income-tax Officer shall make such inquiry thereinto as he may think fit, and, if he is satisfied that the joint family property has been partitioned among the various members or groups of members in definite portions he shall record an order to that effect:

Provided that no such order shall be recorded until notices of the inquiry have been served on all the members of the family.

(2) Where such an order has been passed, or where any person has succeeded to a business, profession or vocation formerly carried on by a Hindu undivided family whose joint family property has been partitioned on or after the last day on which it carried on such business, profession or vocation, the Income-tax Officer shall make an assessment of the total income received by or on behalf of the joint family as such, as if no partition had taken place, and each member or group of members shall, in addition to any income-tax for which he or it may be separately liable and notwithstanding anything contained in sub-section (1) of Section 14, be liable for a share of the tax on the income so assessed according to the portion of the joint family property allotted to him or it;

and the Income-tax Officer shall make assessments accordingly on the various members and groups of members in accordance with the provisions of Section 23:

Provided that all the members and groups of members whose joint family property has been partitioned shall be liable jointly and severally for the tax assessed on the total income received by or on behalf of the joint family as such.

(3) Where such an order has not been passed in respect of a Hindu family hitherto assessed as undivided, such family shall be deemed, for the purposes of this Act, to continue to be a Hindu undivided family.

26. (2) Where a person carrying on any business, profession or vocation has been succeeded in such capacity by another person, such person and such other person shall, subject to the provisions of sub-section (4) of Section 25, each be assessed in respect of his actual share, if any, of the income, profits and gains of the previous year :"

Under the Act of 1918 assessment was made on the income of the year of assessment but by the Act of 1922 the "previous year" was made the basis of assessment. Thus in many instances a business, profession or vocation which had been taxed under the Act of 1918 in the year of assessment was also taxed under the Act of 1922, the assessment year of the Act of 1918 becoming the previous year under the Act of 1922. To avoid double taxation on the income of the same period the Act provides that where a business, profession or vocation on which income-tax was paid under the Act of 1918 is discontinued or where the person who was carrying on any such business, profession or vocation is succeeded by another person, the income, profits and gains of the period commencing from the date of expiry of the previous year to the date of discontinuance or succession is not to be taxed. This is the principle underlying Section 25 but its application to the facts of a particular case presents several aspects. The marginal note of the section is "Assessment in case of discontinued business" but an analysis of its provisions leads to the following results :—

(1) Generally the income which has to be taxed is the income of the previous year. But if a business is discontinued the section, contrary to the general rule, gives to the Income-tax Officer the power to make assessment in the year of assessment on the basis of the income, profits or gains of the assessment year in addition to the assessment, if any, of the previous year. Thus the period of income, profits and gains of which may be assessed, in such a case, is the period for which the business was carried on after the expiry of the previous year, or such period and the previous year if not already assessed, though in the latter case the income for each of these periods has to be separately assessed by the same order (sub-section 1).

(2) It may be that the business that has been discontinued in a particular year was a business on which tax was charged under the Act of 1918. In such a case the section provides that tax shall not be payable in respect of the income, profits and gains of the period for which the business was carried on after the end of the previous year. The section further provides that in such a case the assessee may claim that the income of the previous year shall be deemed to have been the income of the period for which the business was carried on after the end of the previous year. Where the assessee makes such a claim, the income of the period for which the business was carried on after the

end of the previous year shall be assessed and if the tax payable on it is less than the tax paid or payable on the income of the previous year the excess shall be refunded or allowed, as the case may be, to the assessee (sub-section 3).

(3) It may be that a business which was charged to tax under the Act of 1918 is not discontinued but is passed on to another person, the person carrying it on in the past completely severing his connection with it. In such a case, the section provides that the person transferring the business may claim the same benefit as a person whose business has discontinued (sub-section 4).

The important point to remember about Section 25 is that the period, the income of which has to be assessed, is not only the previous year but the previous year and the period for which the business was carried on after the end of the previous year before its discontinuance or succession and that it looks at the position of the person discontinuing or transferring the business from the point of view of his having paid income-tax on that business under the Act of 1918. Where no tax was paid under the Act of 1918 assessment may be made on the income not only of the previous year but also on the income of that portion of the year of assessment for which the business was carried on. But where the person discontinuing the business was also charged under the Act of 1918, though the period, the income of which has to be assessed, remains the same, namely, the previous year and that portion of the year of assessment for which the business was carried on, a special rule for determining the tax payable on the income of this period has been enacted. It is not necessary that the business should have been totally discontinued; what has to be seen is whether the person who carried on the business in the previous year has severed his connection with it after the previous year either by discontinuing it or by assigning it to someone else. It is, therefore, clear that the section is intended to meet only those cases where business has been carried on after the end of the previous year and before the expiry of the year of assessment and looks at the situation from the point of view whether or not any tax on such business was paid under the Act of 1918.

Unlike Section 25, Section 25-A deals with an entirely different position. It says nothing about the chargeability of a business under the Act of 1918 and the period the income of which has to be taxed is the normal period, namely, the previous year. It envisages a position where at the time of making an assessment on the income of the previous year the Income-tax Officer finds or it is alleged before him that the family which was in the past assessed as an undivided Hindu family exists no longer, having partitioned its property or that the business, profession or vocation hitherto carried on by a Hindu undivided

family has passed on to someone else and the family has also disrupted and partitioned its property after the assignment of the business. The section provides that in such a case the income of the family during the period that it carried on the business as an undivided family shall be assessed, and the tax payable on it levied on the members or groups of the family according to the portion of the joint family allotted to them. Thus the subject-matter of this section is wholly different from the subject-matter of the preceding section and each of these sections deals with an entirely different set of circumstances. There is no inconsistency, repugnancy or contrariety between them nor do they overlap each other. Each deals with a different position and enacts a different rule. As pointed out in *Ram Rakha Mal & Sons Ltd.* v. *Commissioner of Income-tax, Punjab* [1], each section in the Income-tax Act deals only with the matters specified therein and goes no further and each section completely covers the matters with which it deals. Interpreted in this way each of these two provisions appears to me to deal with an entirely different subject.

The only relevant provision in Section 26 is sub-section (2) which deals with cases where there has been succession to a business, profession or vocation and provides that the income of each of the persons, namely, the person carrying on the business, profession or vocation in the past and his successor shall be assessed in respect of his actual share in the income, profits and gains of the previous year. There is some overlapping between this sub-section and sub-section (2) of Section 25-A, where an undivided Hindu family has assigned its business to someone else in a particular year and has also disrupted and partitioned its property after the assignment. The case apparently comes under sub-section (2) of Section 26 because *ex hypothesi* during that year the business was carried on by the family for a portion of the year and by the successor for the remaining portion of the year. Sub-section (2) of Section 25-A also is applicable to cases where there has been a succession to the business of an undivided Hindu family and a subsequent partition. Therefore both these sub-sections would apply to such a situation. But a closer scrutiny of these two provisions would show that the moment it is found that the family has been succeeded in its business and partitioned its property after such succession, the Income-tax Officer must proceed under sub-section (2) of Section 25-A, the provisions of that section being more specific than the provisions of sub-section (2) of Section 26. It has been held by the Privy Council in *Sir Sundar Singh Majithia* v. *Commissioner of Income-tax*[2], that Section 25-A of the Act does not

(1) (1937) 5 I.T.R. 137 ; I.L.R. 18 Lah. 325. (2) (1942) 10 I.T.R. 457.

apply unless there has been a complete disruption and partition of the whole of the property of an undivided Hindu family and that the mere transfer of a business by the family without complete partition of its property does not invite the application of that section. Cases are, therefore, possible where an undivided Hindu family might assign its business which is only one of its assets and retain a joint status in respect of all other assets. To such a case Section 25-A will not be applicable and the Income-tax Officer will have to proceed under sub-section (2) of Section 26. The assessee under Section 25-A is the members or groups of the quondam undivided Hindu family whereas under sub-section (2) of Section 26 the assessee is the family itself because *ex hypothesi* the family exists though one of its assets, namely, the family business, has been transferred. It seems to me, therefore, that there is really no conflict between sub-section (2) of Section 26 and sub-section (2) of Section 25-A and that the former deals with those residuary cases where the family has not partitioned its entire property though its business has been transferred to someone else. The assessee under sub-section (2) of Section 26 is the undivided family in respect of the income earned by it from such business whereas under sub-section (2) of Section 25-A, the assessee is the members of the quondam Hindu undivided family. There is thus no conflict between these two sub-sections each of which provides for an entirely different position.

It is admitted that if the case be covered by sub-section (2) of Section 26, the family would be entitled to the relief claimed. It is further admitted that, so far as the right to the relief claimed is concerned, there is no real difference of principle between the cases covered by sub-section (2) of Section 26 and those where the assessment has been made under sub-section (2) of Section 25-A. It is, however, contended that since the provisions of sub-section (2) of Section 26 are made expressly subject to the provisions of sub-section (4) of Section 25 and there is no such reservation in cases where the Income-tax Officer proceeds under sub-section (2) of Section 25-A, the legislature must be deemed to have impliedly negatived the right to relief where the family has disrupted and partitioned its property. If there had been an express provision to the effect that a Hindu family after disruption and partition of its property is not entitled to the benefit of sub-section (4) of Section 25, or even if this conclusion had been implicit in the statute, it would have been our duty to negative the right to relief irrespective of whether there was or was not any reason for the disallowance of such relief. But it is conceded that there is no such express provision, and I am unable to hold

that there is in the statute any necessary implication that whereas a family which retains its undivided status at the time of the assessment, though it has transferred one of its assets, namely the family business, is entitled to the benefit of sub-section (4) of Section 25, no such right to relief exists in cases where the family having completely disrupted itself and partitioned all its property does not exist at the time of the assessment. Emphasis was laid by the learned counsel for the Commissioner on the difference in the phraseology of sub-section (3) and sub-section (4) of Section 25 and it was contended that whereas the word used in the former is "assessee," the words used in sub-section (4) are "such person." This difference in the terms of these sub-sections was, in my opinion, necessary and is an argument against the contention of the learned counsel for the Commissioner rather than an argument in his favour. It must be remembered that in cases contemplated by sub-section (3), the business having been discontinued, the assessment has to be made on the person who carried on such business during a portion of the year and therefore the assessee is that person. In cases contemplated by sub-section (4) of Section 25, however, the assessee may not be the person who has transferred the business. The right to relief under this sub-section vests only in the person who has been succeeded in the business who may not necessarily be the assessee. For instance, in this very case, the assessment being under sub-section (2) of Section 25-A, the assessees are the persons who constituted the undivided family, but the right to relief vests in the undivided family whose income has to be assessed under that sub-section. The use of the word "assessee" in this sub-section would clearly have been incorrect, and, if that word had been used the sub-section would not have applied to cases where the person transferring the business was not the assessee. This difference, therefore, in the language of sub-sections (3) and (4) is, in my opinion, intentional and cannot lead to the inference that the right to relief can only be claimed by an assessee and that where an undivided Hindu family ceases to exist as such after disruption and partition of its assets, the sub-section ceases to be applicable. In my opinion, it is impossible to find any reason to exclude a quondam Hindu undivided family from the benefit of sub-section (4) and no such reason beyond the fact that the family no longer exists as undivided has been advanced. Where, as in this case, no question of refund of the tax paid on the income of the previous year arises, the Act makes it incumbent on the Income-tax Officer not to tax the income of the period between the end of the previous year and the date of succession. It is not necessary that any claim for such exemption should be made, and, therefore, nothing turns on the circumstance that at the

time of assessment the person entitled to the exemption is not in existence. The case is fully embraced by the provisions of the sub-section and I am unable to discover anywhere in the Act any express or implied provision to a contrary effect. The contention raised before us was put forward on behalf of the Commissioner in the Madras Full Bench case, *Kotha Govindarajulu Chettiar* v. *Commissioner of Income-tax, Madras*[1], but it was repelled and all the five Judges who constituted that Bench agreed that notwithstanding the partition, the assessee's family, by virtue of Section 25-A, must be regarded as joint for the purposes of assessment, which must include the grant of relief under Section 25 (4). In my opinion, therefore, the decision of the Tribunal was correct and the answer to the question formulated must be against the Commissioner. My answer to the question formulated is that where an assessment has been made under sub-section (2) of Section 25-A on the members of a Hindu divided family, the family which carried on the business as an undivided family during a portion of the year before its succession is entitled to relief under sub-section (4) of Section 25. The family will have its costs of the reference.

SALE, J.—I agree.

DIN MOHAMMAD, J.—The circumstances in which this case was stated by the Income-tax Appellate Tribunal and the reasons for which, while sitting as a member of a Division Bench, I decided to refer one of the two questions propounded by the Tribunal to a larger Bench, are fully set out in my order, dated the 14th April, 1944, and need not be recapitulated. Suffice it to say that the short question that falls for determination at this stage is whether in the circumstances of this case the assessee cannot legally claim the benefit of sub-section (4) of Section 25 of the Income-tax Act, on account of the provision of law newly introduced in 1939 in sub-section (2) of Section 25-A as regards succession to a business carried on by a Hindu undivided family.

The reply to this question depends upon the true construction to be put upon sub-section (2) of Section 25-A in the light of the other provisions of the statute that are closely connected with it. Prior to the amendment of 1939 Section 25 was headed "Assessment in case of discontinued business" and Section 25-A "Assessment after partition of a Hindu undivided family." After the amendment, although the headings of both these sections were left intact, their subject-matter was extended beyond their scope. Sub-section (4) was added to Section 25 despite the fact that it dealt with succession to a business,

(1) (1944) 12 I. T. R. 97; I.L.R. 1944 Mad. 504.

profession or vocation on which tax was at any time charged under the provisions of the Indian Income-tax Act, 1918 (VII of 1918), and sub-section (2) of Section 25-A was so amended as to include the case of a person who "has succeeded to a business, profession or vocation formerly carried on by a Hindu undivided family whose joint family property has been partitioned on or after the last day on which it carried on such business, profession or vocation." It is obvious that having regard to the limited scope of the headings of these sections the matter of succession could not be properly inserted therein. This defect in drafting is mainly responsible for the difficulty that has arisen in the interpretation of these provisions. On behalf of the Commissioner of Income-tax it is contended that in view of the new provision of law introduced in sub-section (2) of Section 25-A all cases of succession to an undivided Hindu family should be governed by this sub-section. In my view, however, this argument suffers from more defects than one. Firstly, it runs counter to the well-established principle of the interpretation of statutes that when once a legislature has made a special provision about a certain class of cases, any general provision of law cannot derogate from it. Sub-section (4) of Section 25 dealt with all kinds of succession to any business, profession or vocation on which tax was at any time charged under the provisions of the Indian Income-tax Act, 1918 (VII of 1918). Consequently when the legislature enacted the new provision in sub-section (2) of Section 25-A, it could not in any manner prejudicially affect or come into conflict with the provision already made in sub-section (4) of Section 25. Secondly, it offends against another well-recognised principle of the interpretation of statutes that a legislature should not be presumed to have laid itself open to the charge of inconsistency in the same statute in enacting conflicting provisions of law. Courts should always make a genuine effort to reconcile the various provisions that exist in the same statute touching the same subject and to presume that the legislature has been reasonable and consistent in this connection. I may also refer to the following observations made by me in *Ram Rakha Mal* v. *Commissioner of Income-tax, Punjab* [1] :—

"Considering that in the matter of the interpretation of statutes, our first effort should be to reconcile the various provisions of an enactment with one another and to assign to the clear words of a statute the meaning which they ordinarily carry and thinking at the same time that the legislature has not been guilty of redundance of expression or repetition of subjects, the irresistible conclusion to which we are driven is that so far as the scheme of the Act goes, (a) each

(1) (1937) 5 I.T.R. 137, at p. 151; I.L.R. 18 Lah. 325, at p. 333.

section deals only with the matters specified therein and goes no further, and (b) each section completely covers the matter with which it deals."

Thirdly, if effect is given to the interpretation suggested on behalf of the Commissioner of Income-tax, grave injustice will result inasmuch as without any rhyme or reason a Hindu undivided family otherwise entitled to the benefit of sub-section (4) of Section 25 will at once be deprived of it. Sitting as a Court of law we should always guard against all inequitable consequences and put such construction on the statute as to avoid them.

Interpreted in this manner, the new provision of law introduced in sub-section (2) of Section 25-A will not debar the assessee from claiming the benefit of sub-section (4) of Section 25. I would accordingly answer the question propounded by the Tribunal in the negative and grant the family its costs.

MEHR CHAND MAHAJAN, J.—In my opinion the question, "whether on the facts of the case, the application of Section 25-A (2) is a bar to the assessee's claim either under Section 25 (4) or Section 25 (3)," should be answered in the negative. Shortly stated my reasons in support of the answer are these :—

Section 25-A (2) by a statutory command keeps alive the joint Hindu family for the purpose of making an assessment in spite of the fact that it has ceased to exist and the fact of the partition of its property has already been recognized by the Income-tax Officer under sub-section (1) of Section 25-A. An assessment can be made on the total income of the joint family as such as if no partition has taken place ; in other words, it is deemed to be alive for the purpose of determining the assessable income. Once an assessment order is made in the manner required by sub-section (2) of Section 25-A then the amount of the tax can be realized jointly or severally from the persons who were its members before the partition. For purposes of payment of the tax the joint liability of the ex-members of the family still continues and this can only arise on the hypothesis that the family is deemed to exist in spite of partition even for this purpose, as on no other principle can a tax assessed on various members or groups of members separately be recovered jointly from all of them. The true scope of Section 25-A (2) in my view is that it amplifies, and extends the ambit of Section 23, the assessment section, and authorises the assessing officer in making the assessment to assess a joint Hindu family after it has disrupted by ignoring the partition. If my reading of the section is correct then it is obvious that it in no way conflicts with the provisions of Section 25 (4) which are intended to grant relief in

respect of double tax paid by persons who were assessed under the Act of 1918 and were also charged advance tax when the Act of 1922 came into force. The two sections, namely, Sections 25-A (2) and 25 (4) deal with different subjects; the former was not intended to operate as an exception to the latter so as to deprive an undivided Hindu family, one of the taxable units under the Act, from its benefit. It could not be the intention or the object of the legislature that relief in respect of double tax already charged should only be allowed to three out of the four taxable identities dealt with by the Act. I cannot ascribe to the legislature an intention to the effect that it wished to discriminate between the different persons liable to the charge of income-tax under Section 3 of the Act and that its object was to give relief and confer benefit on all these units excepting an undivided Hindu family in whose case it somehow considered that the advance tax paid by it on its business in the year 1922 should be forfeited.

Further, I think that Section 25-A and Section 26 (2) are not mutually exclusive. As observed by their Lordships of the Privy Council in *Commissioner of Income-tax* v. *Polson*[1], Section 26 is primarily directed not to the circumstances in which relief for taxation is given but to the apportionment of tax where relief is not given. This section, therefore, does not in any way affect the contention of the assessee.

As the undivided Hindu family is deemed to continue for the purposes of assessment, in making the assessment under Section 25-A, relief under Section 25 (4) can properly be given. This relief was rightly allowed by the Tribunal in this case as the business of the joint family was assessed to tax under the Income-tax Act of 1918 and there being a succession to the business, the joint family was entitled to the benefit of the relief conferred by Section 25 (4) of the Act of 1922. The undivided family stands on the same footing as any other taxable unit. In my judgment there is no inconsistency, repugnancy or conflict between the provisions of Sections 25 (4), 25-A and 26 of the Act. Each one of them deals with specific subjects and does not in any way run counter to the other, though they all form part of a single scheme. For these reasons, I agree that the question referred be answered in the negative.

KHOSLA, J.—The facts of this case are given in detail in the very lucid judgment of my learned brother Munir, J., and need not be repeated here. The question referred to the Full Bench was: "Whether, on the facts of the case, the application of Section 25-A (2) is a bar to the assessee's claim either under Section 25 (4)

(1) (1945) 13 I.T.R. 384; 49 C.W.N. 786.

or Section 25 (3)." Section 25 and Section 25-A occur in Chapter IV of the Income-tax Act. Chapter IV deals with assessments and deductions, that is, the manner in which taxable income is to be assessed and the tax thereon recovered. A reading of the various sections in this chapter shows that the scheme of the Act was intended to cover the various types of assessment that arise in actual practice. In this chapter an answer is provided to the questions, who is to be assessed, for what period is the assessment to be made and from whom is the tax to be recovered. Directions for dealing with the case of a business which is discontinued or transferred and the case of a joint Hindu family after partition are set out. Upon a plain interpretation it is seen that there is nothing in Section 25-A repugnant to Section 25 (4) of the Act.

Section 23 describes in general terms the mode of assessment. This section applies to all assessees, whether the assessee be a firm or a Hindu undivided family. Sections 24, 24-A and 24-B deal with matters which are not relevant to the present enquiry. Section 25 deals with assessment in the case of a business which has been discontinued or transferred. Section 25-A deals with assessment of a Hindu undivided family after it has been partitioned, and Section 26 covers the case of a change in the constitution of a firm.

A proper understanding of these sections will be facilitated by considering a few instances. The case of a firm which came into existence after 1918 does not present any difficulty, for to such a firm Section 25 (3) and (4) do not apply. Such a firm will be assessed under Section 23 and if it is discontinued or is transferred Section 25 (1) and (2) will cover the case. The case of a joint Hindu family business started after 1918 too does not involve complexity. Suppose a joint Hindu family is partitioned in a certain year, then under the provisions of Section 25-A the business will be taxed up to the date of its discontinuance and the tax will be recovered from various members. The family will be assumed to continue as joint for the purpose of assessment only.

Now, consider the case of a business started before 1918. Suppose in a certain year X the business is discontinued. In this year an assessment for the previous year, that is, for the year X-1 will be made. Another assessment will be made for the broken period of the year X, that is, from the end of the year X-1 up to the date of discontinuance. Under the provisions of Section 25 (4) no tax is payable in respect of the broken period in the year X. Section 25 (4) further provides that if this tax of the broken period in the year X is less than the tax in the year X-1, the firm will be allowed a rebate. The case of a joint family business is to be treated in the same way. If the

business is discontinued in the year X the same method of assessment will apply and relief will be given under Section 25 (4). Now, supposing the joint family is partitioned and the business is, therefore, discontinued or transferred to one of its members and if this partition takes place in the year X, the mode of assessment will be exactly similar to the mode employed in assessing a firm. In this year the assessment for the year X-1 will be made under the provisions of Section 25-A. Relief will be permissible under the provisions of Section 25 (4) in the same way as if the joint Hindu family business had been an ordinary business which was discontinued in the year X. In the year X-1 assessment will be made according to the provisions of Section 26.

Now, apply these principles to the facts of the present case. In the year 1941-42 the family was partitioned and an application under Section 25-A of the Income-tax Act was made. The assessment for the previous year will be made as if the family were still undivided according to the provisions of Section 25-A and the tax assessed will be recovered from the various members of the joint family. For the portion of the next year (18th April 1940—25th March 1941) an assessment will be made and relief will be given according to the provisions of Section 25 (4). There is nothing in Section 25-A which is repugnant to the provisions of Section 25 (4). Section 25-A merely provides the mode of assessing a joint Hindu family which has been partitioned. It does not cover the case of the relief permissible under Section 25 (4) which is confined to those firms which were taxed under the Income-tax Act of 1918. Section 25-A covers the case of all joint Hindu families whether they were paying tax under the 1918 Act or not. The specific matter dealt with under Section 25 (4) not being inconsistent with the general topic of Section 25-A, relief must be given under Section 25 (4). I would accordingly answer the question referred to the Full Bench in the negative.

Reference answered accordingly.

[IN THE NAGPUR HIGH COURT.]

INCOME-TAX APPELLATE TRIBUNAL, BOMBAY

v.

B. P. BYRAMJI AND CO.

GRILLE, C. J., and PURANIK, J. July 23, 1945.

INDIAN INCOME-TAX ACT (XI OF 1922 AS AMENDED IN 1939), SEC. 34—RE-ASSESSMENT—"DEFINITE INFORMATION," MEANING OF—MISTAKE OF LAW—WHETHER ASSESSMENT CAN BE RE-OPENED.

Under Section 34 of the Indian Income-tax Act, 1922, as amended in 1939, the Income-tax Officer has no power to re-open an assessment unless he acts in consequence of definite information which has come into his possession. A mistake of law is not a ground for re-opening the assessment.

An Income-tax Officer took the view for the charge year 1939-40 that the rates at which super-tax should be charged by virtue of the provisions of Section 6 (4) (v) of the Finance Act, 1939, were the rates prescribed by the Finance Act, 1938, and he made an assessment accordingly. The successor to that officer however took the view that the rates of the Finance Act, 1939, should have been applied and he sought to re-open the assessment under Section 34 of the Indian Income-tax Act as amended in 1939 :

Held, *that the view of the successor, even though it was correct, was not based on any definite information coming into his possession but he only corrected a mistaken view of the law applicable, setting his own opinion against that of his predecessor, and that was not a sufficient ground for re-opening the assessment under Section 34 as amended in 1939.*

Cases referred to :

British Sugar Manufacturers Ltd. *v.* Harris [1938] (16 A.T.C. 421 ; [1938] 2 K. B. 220; 21 Tax Cas. 528 ; 7 I.T.R. 101 ; (1938) 1 All E.R. 149).

Commissioner of Income-tax, Madras *v.* Lakshmana Iyer [1945] (13 I.T.R. 242 ; A.I.R. 1945 Mad. 329 ; (1945) 1 M.L.J. 383).

Commissioner of Income-tax, Bengal *v.* Mahaliram Ramjidas [1940] (A.I.R. 1940 P.C. 124 ; 189 I.C. 154 ; I.L.R. [1940] 2 Cal 215; 67 I.A. 239 ; 8 I.T.R. 442).

Commissioner of Income-tax, Bombay *v.* Sir Mohamed Yusuf [1944] (12 I.T.R. 8 ; I.L.R. 1944 Bom. 230 ; 214 I.C. 267 ; A.I.R. 1944 Bom. 160).

Commissioner of Income-tax, Bombay *v.* D. R. Naik [1939] (7 I.T.R. 362 ; 184 I.C. 836 ; A.I R. 1939 Bom. 362 ; I.L.R. 1939 Bom. 445).

Raghavalu Naidu & Sons *v.* Commissioner of Income-tax, Madras [1945] (13 I.T.R. 194 ; A.I.R. 1945 Mad. 311 ; (1945) 1 M.L.J. 296).

Williams *v.*Grundy [1934] (2 I.T.R. 236 ; 103 L.J.K.B. 204 ; 18 Tax Cas. 271).

Reference under Section 66 (1) of the Indian Income-tax Act (XI of 1922) by the Income-tax Appellate Tribunal, Bombay: Miscellaneous Civil Case No. 36 of 1944.

STATEMENT OF CASE.

" Under Section 66 (1) of the Indian Income-tax Act, 1939, we are submitting this reference at the instance of the assessee, Messrs. B. P. Byramji & Co., whose application in this connection is marked Exhibit A in the appended list. The Commissioner of Income-tax, U. P., C. P. & Berar, has filed a written answer, Exhibit B.

2. We shall presently formulate the two questions that we propose to submit to their Lordships. Broadly speaking, the point is

whether the re-opening of the assessee's assessment for the charge year 1939-40, under Section 34 of the Act, is valid. It arose before us in the following circumstances.

3. The assessee was assessed for the charge year in question upon a total income of Rs. 54,024 from different sources. More than half of the total income was derived from dividends. In such a case the Finance Act of 1939 gave a concession to an assessee, such as the applicant, by directing that income-tax and super-tax should be calculated at the rates prescribed by the Finance Act of 1938, under certain conditions. In this case we were concerned with the calculation of super-tax alone, and the particular condition laid down in that connection was that super-tax had either been deducted in the account year under the Income-tax Act of 1922, or would have been so deductible if the Indian Income-tax Act, 1939, had come into effect on 1st April 1938. The Income-tax Officer who made the first assessment applied the older rates thinking that the assessee's case satisfied all the necessary conditions. Later, however, his successor in office, on looking into the record, thought that the older rates had been wrongly applied and that the assessee's total income attracted the application of the rates of super-tax prescribed by the Finance Act, 1939. He accordingly re-opened the assessment for the purposes of super-tax alone and levied the amount at the rates prescribed by that Act. The assessee took successive appeals to the Appellate Assistant Commissioner and the Tribunal. He raised several contentions in his respective memos of appeals, but they are not material to the present purpose. Before the Tribunal, however, he raised an additional ground that his re-assessment under Section 34 was illegal inasmuch as it amounted to a revision of the assessment made by the first Income-tax Officer. The point was not however taken in the memo of appeal but by a separate letter. We did not permit it to be taken and argued in the appeal. On a reference to their Lordships, they held that the point ought to have been considered by us and directed that it should be heard. Accordingly, the appeal was re-heard. A copy of our judgment is Exhibit C.

4. In paragraph 5 of our judgment we have made it clear that the Income-tax Officer who re-opened the assessment under Section 34 of the Act thought the first Income-tax Officer had committed an error of law in applying the older rates of super-tax prescribed by the Finance Act of 1938, and that he re-opened the assessment on the information furnished by the record itself. We thought that the information furnished by the record amounted to "definite information" within the meaning of Section 34 of the amended Act of 1939, and, consequently, held that the re-assessment was validly made. The assessee also

contended before us that the re-opening of the assessment for the purposes of super-tax alone was precluded by the provisions of Section 56 of the Act. On that point, too, we held against him. Our reasons for both the conclusions are recorded in paragraphs 4 and 5 of our judgment.

5. Both sides agree that the three questions formulated in the application arise for reference. But we think that the first two may be suitably combined into one and that the third expressed in a somewhat different form. Accordingly, we formulate the following two questions of law for their Lordships' opinion :—

Questions referred—(1) Whether, in the circumstances of the case, the Income-tax Officer who re-opened the assessment had definite information within the meaning of Section 34 of the Indian Income-tax Act, 1939, that the assessee had been assessed to super-tax at too low a rate?

(2) Whether the second Income-tax Officer was by virtue of the provisions of Section 56 of the Act precluded from re-opening the assessment only for the purposes of super-tax, the assessment made by the first Income-tax Officer having become final for the purposes of income-tax?"

V. R. Sen, for the Commissioner.

S. P. Kotval, for the assessee.

JUDGMENT.

On being asked by us to state a case, the Income-tax Appellate Tribunal, Bombay, has referred the following questions :—

"(1) Whether, in the circumstances of the case, the Income-tax Officer who re-opened the assessment had definite information within the meaning of Section 34 of the Indian Income-tax Act, 1939, that the assessee had been assessed to super-tax at too low a rate?

(2) Whether the second Income-tax Officer was by virtue of the provisions of Section 56 of the Act precluded from re-opening the assessment only for the purposes of super-tax, the assessment made by the first Income-tax Officer having become final for the purposes of income-tax?"

The second question was not argued, and it was agreed that the question there posed would stand or fall by the decision on the first question.

The point is a simple one. The income of the assessee firm for the charge year 1939-40 was computed at Rs. 54,024 for the purposes of income-tax and super-tax. The officer who made the original assessment came to the conclusion that the rate at which super-tax should be charged by virtue of the provisions of Section 6 (4) (v) of the

Finance Act of 1939 should be the rate prescribed by the Finance Act of the year before, namely 1938, and the assessment was accordingly so made on March 16, 1940. In the following July, the successor in office of the assessing officer informed the assessee that he proposed to re-assess the income in consequence of definite information that had come into his possession. It is admitted that the "definite information" consisted only of his view of the law as to whether the rates of the Finance Act of 1938 or 1939 were applicable and that in his view, the rates in the latter Act should have been applied. It is not now disputed, as the matter has been finally decided, that in fact the view of the second officer of the law is correct. The question then is whether he had the right, under Section 34, to re-open the assessment.

In its judgment (Ex. T-C) the Income-tax Appellate Tribunal, Bombay, held that the Income-tax Officer could legally re-open the assessment made by his predecessor simply on the ground that the first Income-tax Officer had committed a mistake of law in determining the amount of tax. The Tribunal based its decision briefly on the decision in *Commissioner of Income-tax, Bombay* v. *D. R. Naik*[1], and they referred to a series of English decisions based on *Williams* v. *Grundy*[2] in support of the view that it was not necessary for the Income-tax Officer to possess himself of any outside information. The Bombay decision is based on Section 34 of the Income-tax Act as it stood before the amendment of the year 1939, and it is not disputed before us that it is the amended section, as it now stands, that applies. The pertinent part of that section, before the amendment of 1939, read as follows :—

"If for any reason income, profits or gains chargeable to income-tax has escaped assessment in any year or has been assessed at too low a rate, the Income-tax Officer may, at any time within one year of the end of that year, serve on the person liable to pay tax on such income, profits or gains, or, in the case of a company, on the principal officer thereof, a notice containing all or any of the requirements which may be included in a notice under sub-section (2) of Section 22 and may proceed to assess or re-assess such income, profits or gains, and the provisions of this Act shall, so far as may be, apply accordingly as if the notice were a notice issued under that sub-section."

As it now stands after amendment, it is as follows :—

"If in consequence of definite information which has come into his possession the Income-tax Officer discovers that income, profits or gains chargeable to income-tax have escaped assessment in any year, or have been under-assessed, or have been assessed at too low a rate, or have been the subject of excessive relief under this Act, the Income-

(1) (1939) 7 I.T.R. 362. (2) (1934) 2 I.T.R. 236.

tax Officer may, in any case in which he has reason to believe that the assessee has concealed the particulars of his income or deliberately furnished inaccurate particulars thereof, at any time within eight years, and in any other case at any time within four years of the end of that year, serve on the person liable to pay tax on such income, profits or gains, or, in the case of a company, on the principal officer thereof, a notice containing all or any of the requirements which may be included in a notice under sub-section (2) of Section 22, and may proceed to assess or re-assess such income, profits or gains, and the provisions of this Act shall, so far as may be, apply accordingly as if the notice were a notice issued under that sub-section."

It is obvious that by the amendment, the Income-tax Officer has no power to re-open an assessment unless he acts in consequence of definite information which has come into his possession. Now, while a mistake of law might have been permissible as a ground for re-opening an assessment before the amendment of 1939, we are satisfied that that cannot be the case now. It is urged on behalf of the Commissioner of Income-tax that definite information can be obtained from a book, and that the information on which action was taken was derived from a more careful reading of the Act than that made by the first assessing officer. This is not definite information at all. It amounts to nothing more than a change of opinion on the part of the authority making the assessment. The second opinion might be right or it might be wrong, and the fact that the second opinion has, in the event, been held to be right is irrelevant. On the argument put before us, there was nothing to prevent a third assessing officer, assuming that the incumbency of the post had changed once more, from re-opening the case yet again and coming to yet another conclusion on a matter of opinion. A fact discovered in consequence of definite information need not necessarily be a concrete fact as to a certain amount of income undiscovered. A discovered fact might also be a decision of a Court of law which was not available at the time of the first assessment or a provision of statute enacted since the first assessment. It might even conceivably arise in (we do not say that it does) a case where a statute had escaped the notice of the earlier assessing officer. This obviously cannot be the case here as both officers acted on the same Act, namely, the Finance Act of 1939.

There has been a consensus of judicial opinion that since the amendment of 1939, a mistake of law will not permit the re-opening of an assessment under Section 34 of the Act. We would refer in particular to *Commissioner of Income-tax, Bombay* v. *Sir Mohamed Yusuf* [1],

(1) (1944) 12 I.T.R. 8.

where the case of *Commissioner of Income-tax, Bombay* v. *D. R. Naik* [1], was cited and not followed. The reason is clearly that the amended Act had caused that decision to be invalid, and it is pertinent to note that Beaumont, C. J., was a party to both decisions. The principle is also stated by the Madras High Court in *Raghavalu Naidu & Sons* v. *Commissioner of Income-tax, Madras* [2], and that decision is affirmed by a later case in the same Court in *Commissioner of Income-tax, Madras* v. *Lakshmana Iyer* [3].

Reliance has been placed on behalf of the Commissioner on a Privy Council decision in *Commissioner of Income-tax, Bengal* v. *Mahaliram Ramjidas* [4], for the proposition that the provisions of the Income-tax Act should be so interpreted as to make the machinery workable. No difficulty of this nature arises in the case before us since the only point at issue is the interpretation of the words "definite information." Finally it is contended that the cases we have cited are not good law and that the English decisions based on *Williams* v. *Grundy* [5] should be followed in interpreting even the revised Section 34. This argument can be of no avail. The corresponding provision in the English Act begins with the words, "If the surveyor discovers that . . . have been omitted from the first assessment, etc." and the English decisions are based on the interpretation of the word "discovers." There is, in the English Act, no such restriction as is raised in the opening words of Section 34, "If in consequence of definite information which has come into his possession," and we may also add that on the very narrow point before us, namely, the mere discovery of the fact of under-assessment, the decision of *Williams* v. *Grundy* [5], was doubted by the Court of Appeal in *British Sugar Manufacturers Ltd.* v. *Harris* [6], as pointed out by Beaumont, C.J., in *Commissioner of Income-tax, Bombay* v. *Sir Mohamed Yusuf* [7].

The view of the Income-tax Officer who re-opened the assessment, even if correct, was not based on any definite information coming into his possession and he only corrected a mistaken view of the law applicable, setting his own opinion against that of his predecessor. This is not a sufficient ground for re-opening an assessment. We answer the question in the negative and the result is that the claim succeeds. The Commissioner of Income-tax will pay the costs of the applicant which we assess at Rs. 75, and the applicant is also entitled to a refund of the reference fee of Rs. 100.

Reference answered in the negative.

(1) (1939) 7 I.T.R. 362.
(2) (1945) 13 I.T.R. 194.
(3) (1945) 13 I.T.R. 242.
(4) (1940) 8 I.T.R. 442.
(5) (1934) 2 I.T.R. 236.
(6) (1938) 7 I.T.R. 101 ; 21 Tax Cas. 528.
(7) (1944) 12 I.T.R. 8.

[IN THE LAHORE HIGH COURT.]

NAND LAL BHOJ RAJ, *In re.*

DIN MOHAMMAD and MEHR CHAND MAHAJAN, JJ.

October 2, 1945.

INDIAN INCOME-TAX ACT (XI OF 1922), SEC. 10 (2) (xii)—BUSINESS EXPENDITURE—MANUFACTURE OF SALTPETRE—SUM SPENT IN ACQUIRING LEASES OF SALT BEARING LANDS—WHETHER ALLOWABLE DEDUCTION.

The assessee carrying on a business of manufacturing saltpetre acquired year after year leases of lands containing deposits of crude saltpetre from several persons including Government on contract basis. The period of each lease varied in accordance with the saltpetre available from them. The leases had durations of 5 to 10 years and in certain cases lesser or greater:

Held, *following* PARMA NAND HAVELI RAM, IN RE [1945] (13 I.T.R. 157) *that the moneys spent in acquiring the leases of lands containing deposits of crude saltpetre were revenue expenditure allowable under Section 10 (2) (xii) of the Income-tax Act.*

Case referred by the Income-tax Appellate Tribunal under Section 66 (1) of the Indian Income-tax Act, 1922: Civil Reference No. 25 of 1943.

STATEMENT OF CASE.

"These are three applications, *viz.*, 66 R.A. Nos. 5, 6 and 7 (Punjab) of 1942-43 by the Commissioner of Income-tax, Punjab, requiring us to refer under Section 66 (1) of the Income-tax Act a question of law which is said to arise out of our orders, dated April 21, 1942, in R.A.A. Nos. 63, 64 and 65 (Punjab) of 1941-42.

2. During the proceedings for the assessment year 1938-39 before the Income-tax Officer, the assessee, as usual, claimed as business expenditure under Section 10 (2) (xii) of the Income-tax Act, the money expended by him in acquiring lease of lands for the purpose of extracting saltpetre therefrom. The following extract from the Income-tax Officer's order explains the nature of the claim:—

'The assessee has so far been erroneously enjoying the benefit of the amount spent by him in acquiring the lease of lands from which crude saltpetre is extracted and brought for crystallization to the assessee's refineries installed at Phullarwan. These leases of land are acquired year after year from several persons including Government on contract basis and the period of each lease varied in accordance with the saltpetre available from them. These leases have durations of 5 to 10

years and in certain cases lesser or greater. The assessee has maintained a separate account regarding the leases of lands in which the money invested from time to time and other expenses incurred are credited and debited in accordance with the requirements or duration of the various leases. Out of the net balance in hand proportionate sums of money calculated upon the duration and the amount of the full lease term is charged to the revenue account for determining the assessable income. The lease account for this particular period is as detailed above. A sum of Rs. 17,235 has been debited to the saltpetre account for lease of mounds relevant to the manufacture of saltpetre during the year and the balance of Rs. 25,538 has been carried forward to the next year.'

3. The Income-tax Officer was of the opinion that the facts of the case were on all fours with the facts in *Shanker Shambhaji Gangla* v. *Commissioner of Income-tax, Bombay*[1], *Commissioner of Income-tax, U. P.* v. *Tika Ram & Sons Ltd.*[2], and *U. Chengalvaroya Mudaliar* v. *Commissioner of Income-tax, Madras*[3]. The only distinction that he could see was that the above-mentioned decisions did not relate particularly to saltpetre manufacturers. Relying upon these authorities, the Income-tax Officer concluded that the expenditure in question was in the nature of capital expenditure and rejected the assessee's claim in his assessment order, dated December 20, 1939. Similar claims in respect of the 1939-40 and 1940-41 assessments were rejected on the same reasoning by the relevant assessment orders, dated December 20, 1939, and December 25, 1940, respectively.

4. The assessee preferred appeals to the Appellate Assistant Commissioner, who in his order, dated May 26, 1941, relating to the 1938-39 assessment, upheld the view taken by the Income-tax Officer and repelled the assessee's contentions, relying on the Allahabad High Court's decision in *Commissioner of Income-tax, U. P.* v. *Tika Ram & Sons Ltd.*[2] The appeals on this issue relating to the two subsequent years' assessments were similarly dismissed by the Appellate Assistant Commissioner's orders, dated May 26, 1941.

5. The assessee preferred appeals to the Tribunal against the three above-mentioned orders. By its orders, dated April 21, 1942, in R. A. A. Nos. 63, 64 and 65 (Punjab) of 1941-42, the Tribunal found that the expenditure in dispute in each year was disbursed from the funds set apart by the assessee for the buying of his raw materials and that such expenditure in effect amounts to no more than the purchase of raw materials for the assessee's business of manufacturing saltpetre. In this view the three appeals were allowed by the Tribunal. The

(1) (1936) 9 I. T. C. 350.
(2) (1937) 5 I.T.R. 544.
(3) (1934) 2 I.T.R. 395 ; 7 I.T.C. 323.

present applications arise out of the above-mentioned orders of the Tribunal.

6. The original applications were received on June 25, 1942, and heard on August 12, 1942, in which the findings of fact arrived at by the Tribunal were not questioned as being based on no material. The respondent in his reply pointed out that unless the applicant wanted to say that the findings of fact were not supported by any material on record, no question of law could be said to arise out of the orders of the Tribunal. The Departmental Representative thereupon requested permission to put in amended applications. Permission was granted and the amended applications were presented on September 15, 1942, wherein the applicant questions the existence of material on which the findings of fact arrived at by the Tribunal are based. The applicant further states that in arriving at the findings of fact the Bench of the Tribunal committed an error of law inasmuch as it misinterpreted the provisions of Section 10 (2) (xii) of the Income-tax Act in holding the disputed expenditure as a revenue expenditure. Lastly, it is stated that the Bench of the Tribunal committed an error of law in drawing inferences from the terms of the leases and other evidences on record.

7. In paragraph 4 of his reply filed under rules 53 and 54 of the Appellate Tribunal Rules, the respondent has correctly set out what took place at the hearing and the material upon which the Tribunal found that the expenditure in dispute was incurred out of the funds set apart by the assessee for the purchase of raw materials. The respondent denies that any question of law arises out of the orders of the Tribunal. The finding that such expenditure amounts to no more than the purchase of raw materials for the assessee's manufacturing business is an inference drawn from facts.

8. We are of the opinion that the following question of law arises out of our orders which we refer to the High Court of Judicature at Lahore under Section 66 (1) of the Income-tax Act :—

'Whether in the circumstances found by the Tribunal in which the assessee carries on his business of saltpetre manufacture, the moneys spent in acquiring the leases of lands containing deposits of crude saltpetre have correctly been treated as expenditure in the nature of revenue expenditure allowable as a deduction under Section 10 (2) (xii) of the Income-tax Act.'

The following facts are taken from paras. 1 and 2 of the judgment of the Income-tax Appellate Tribunal delivered under Section 33 of the Income-tax Act :—

'The only point that requires determination is whether the moneys spent for the acquisition of lease of lands containing deposits of crude

saltpetre should be treated as revenue expenditure or whether such expenses are in the nature of capital expenditure. The appellants are a firm of saltpetre manufacturers. The process of manufacture is fairly simple. Crude saltpetre is either bought from the market or extracted from the land acquired for the purpose of removing the saltpetre deposits therefrom. In the latter case earth containing saltpetre is scraped and brought to the manufactory where it is boiled in water. The earth is allowed to settle down and the water is separated in boxes where it crystallises. The position taken up by the appellant is that he finds it cheaper to lease certain lands where crude saltpétre is available and remove the deposit therefrom, than to purchase crude saltpetre from the market. Two specimen leases have been produced before us. One of these leases is between the North Western Railway and the appellant and the relevant portion of it reads as follows :—

"(1) The licensees shall have the use of a piece of railway land measuring . . . for the purpose of extracting crude saltpetre at a rental of Rs. 100 for a period of nine months from 1st April 1941 to 31st December 1941."

"(2) The licensees are permitted to remove saltpetre from the said land to a depth of 2" only from the surface and no pits shall be dug by them."

"(3) The licensees shall under no circumstances erect any structure on the said land."

"(4) No buying or selling shall be carried out by the licensees on the said land and the licensees shall use the said land only for the purpose of the business described in clause (1) above."

2. It is quite clear from the above-mentioned provisions that the licensee does not acquire any rights in the land other than the rights which are strictly ancillary to his business of extracting saltpetre. It is also clear that no process of digging is involved in the operations carried on by him. He is, however, allowed to remove earth to a depth of 2" for the simple reason that the deposit of crude saltpetre cannot be effectively scraped without carrying a little earth with it.' "

Kirpa Ram Bajaj, for the assessee.

S. M. Sikri and *Jindara Lal*, for the Commissioner.

JUDGMENT.

It is agreed that the matter under consideration is covered by the Full Bench decision in Civil Reference No. 12 of 1941.* We accordingly answer the question propounded by the Tribunal in the affirmative. Considering that the question involved was not free from difficulty, we make no order as to costs.

Reference answered in the affirmative.

* Since reported as *Parma Nand Haveli Ram, In re* [1945] (13 I.T.R. 157).

[IN THE MADRAS HIGH COURT.]

COMMISSIONER OF INCOME-TAX, MADRAS

v.

V. E. K. R. SAVUMIAMURTHY.

SIR LIONEL LEACH, C. J., and PATANJALI SASTRI, J.

February 1, 1946.

INDIAN INCOME-TAX ACT (XI of 1922), SEC. 4-B—"NOT ORDINARILY RESIDENT"—"SEVEN YEARS" IN SEC. 4-B—WHETHER REFERS TO SEVEN CALENDAR YEARS OR SEVEN PREVIOUS YEARS.

The expression "seven years" in Section 4-B of the Indian Income-tax Act, 1922, should be taken as referring to the period of seven years of twelve calendar months each immediately preceding the commencement of the relevant previous year and not to the period of seven years ending on the 31st December preceding the commencement of such year.

Case referred to :—

Commissioner of Income-tax, Bombay v. Abubaker Abdul Rahman [1936] (4 I.T.R. 233; 60 Bom. 679 ; 163 I.C. 351 ; 38 Bom. L.R. 450 ; A.I.R. 1936 Bom. 225).

Case stated under Section 66 (1) of the Indian Income-tax Act, XI of 1922, by the Income-tax Appellate Tribunal, Madras Bench, in 66 R.A. Nos. 8 and 9 Madras of 1944-45: Referred Case No. 11 of 1945.

STATEMENT OF CASE.

"These two applications under Section 66 (1) of the Income-tax Act for reference to the Honourable High Court are made by the Commissioner of Income-tax, Madras, from a decision of this Bench dated 28th March 1944, and they arise out of our orders in R. A. A. No. 161 (Madras) of 1942-43 and 14 (1) E. P. T. A. A. No. 26 (Madras) of 1942-43. The question of law framed by the Commissioner is as follows :—

"Whether on the facts found and in the circumstances of this case, the respondent was liable to be assessed as 'ordinarily resident' in British India, on the income arising in Ceylon during the 'previous year' ended 31st March 1940 ?"

2. The facts of the case may be briefly stated as follows :—

The respondent in this case was a Hindu undivided family. It had business in British India as well as in Ceylon. Its income from Ceylon had been added to its income of British India for the purpose of taxation in British India.

3. The accounting year in Ceylon was the financial or official year ending 31st March 1940 and the accounting year in British India

was the Tamil year beginning with 13th April 1939 and ending on 12th April 1940. The respondent contended before us that the status with regard to the residence of the Hindu undivided family depended upon the residence of the karta as contemplated by Section 4-B (a) of the Income-tax Act.

4. The case was sent for enquiry to the Income-tax Officer to find out what number of days the karta, *i.e.*, Mr. Savumiamurthy, was in British India according to (a) the calendar year, (b) Tamil year, and (c) the official or financial year. The Income-tax Officer, on enquiry, sent a report dated 1st November 1942. From that it is found in paragraph 3 that Mr. Savumiamurthy stayed in British India (a) for 541 days, which was accepted by both the parties to be really 606 days, during the period of 7 years from 1st January 1932 to 31st December 1938; (b) for 731 days during the 7 years from Angirasa to Bhahudhanya, *i.e.*, 1932-33 to 1938-39 according to Tamil year; and (c) for 731 days according to the official or financial year.

5. An error of fact seems to have crept in paragraph 2 of our order. While stating the contention of the respondent's Advocate, we said that 'according to the financial year which is the accounting year for Ceylon he has certainly stayed for more than two years.' As a matter of fact, from the Income-tax Officer's report mentioned above, his stay in British India according to the financial or official year was 731 days.

6. The main contention of the respondent before us was that the 'year' mentioned in Section 4-B (a) must be taken to be the calendar year. If that view was to be accepted then clearly he was 'not ordinarily resident' in British India in accordance with that section. He also argued that even if 731 days were to be taken to be his total stay in 7 years according to Tamil or official year, in view of the fact that there must be at least one leap year during that period, it must be taken that 731 days is not more than two years and, therefore, even then he should be taken to be a 'not ordinarily resident' in accordance with that section.

7. Without deciding the question as to whether 731 days would be two years under the circumstances within the meaning of the section, we held that 'year' in the section meant calendar year. We, therefore, found that the respondent was 'not ordinarily resident' in British India, and therefore, could not be taxed with regard to his income in British India as such. We think that a point of law does arise in this case which should be referred to the Honourable High Court. The respondent in this case has objected to the question as framed by the Commissioner. The question framed by him (the

respondent), however, seems to us to be really the question that arises from our order. We, therefore, refer the question as stated by the respondent, *i.e.*,

"Whether, in the circumstances of the case, in computing the period or periods when the manager of the Hindu undivided family had not been in British India, the 'seven years' in Section 4-B of the Income-tax Act should be taken as seven calendar years or seven previous years."

8. It may be stated here that in paragraph 3 (1) of his application under Section 66 (1), the Commissioner has stated that the Bench arrived at the finding that "the respondent is the manager of a 'resident Hindu undivided family' having a business in British India and another business in Ceylon." We do not consider this statement as correct. All that we said in our order was that the respondent had business in British India as well as in Ceylon. We, therefore, refer the question mentioned below to the Honourable High Court.

"Whether, in the circumstances of the case, in computing the period or periods when the manager of the Hindu undivided family had not been in British India, the 'seven years' in Section 4-B of the Income-tax Act should be taken as seven calendar years or seven previous years."

The two applications, one referring to the income-tax assessment and the other referring to the excess profits tax assessment in respect of a portion of the corresponding accounting period, are referred together, at the request of the Commissioner in his applications."

C. S. Rama Rao Saheb, for the Commissioner.

P. R. Srinivasan, for the assessee.

JUDGMENT.

(Judgment of the Court was delivered by Patanjali Sastri, J.)

This reference arises out of an assessment to income-tax and excess profits duty made on the respondent as the manager of a Hindu undivided family for the year 1940-41.

The family was carrying on business at Kakatiruppupudur (Ramnad District) in British India and in Ceylon, and its income from both these sources has been taxed on the footing that the family was "resident" and "ordinarily resident" in British India. In each case the income taxed was of the "previous year," which was the Tamil year Pramathi ending 12th April 1940 for the Indian business and the financial year ending 31st March 1940 for the foreign business, the assessee's accounts in the two places having been made up to those dates

respectively. There was no dispute that the family was "resident" in British India within the meaning of Section 4 (1) (b) read with Section 4-A of the Indian Income-tax Act, 1922, as amended by the Income-tax (Amendment) Act, VII of 1939. The assessee, however, contended that the family was "not ordinarily resident" in British India within the meaning of the second proviso to Section 4 (1) read with Section 4-B and that, accordingly, the income arising to it from the business in Ceylon should not be included in the assessment, there being no suggestion that such business was controlled in India or that such income was brought into British India.

Now, a Hindu undivided family is deemed to be "ordinarily resident" in British India if its manager is ordinarily resident in British India [4-B (b)], and an individual is "not ordinarily resident" in British India in any year "if he has not been resident in British India in nine out of the ten years preceding that year or if he has not during the seven years preceding that year been in British India for a period of, or for periods amounting in all to, more than two years" [4-B (a)]. The assessee's attempt before the Income-tax authorities to prove that his family was not resident in British India in nine out of the ten years prior to the year of account having proved unsuccessful he shifted his position before the Income-tax Appellate Tribunal (Madras Bench) and sought to bring the case under the latter part of the clause (a), contending that the seven years referred to in that clause must be taken to be seven calendar years. The Tribunal ordered a fresh inquiry and it was found (i) that the manager of the family was in British India for 541 (this was subsequently corrected into 606) days on the aggregate during the period of the seven calendar years from 1st January 1932 to 31st December 1938 preceding the year of account whether of the Ceylon or the Indian business, (ii) that he was in British India for 731 days on the aggregate during the seven Tamil years preceding Pramathi, the year of account of the Indian business, and (iii) that he was in British India for 731 days on the aggregate during the seven financial years preceding the financial year 1939-40 which was the year of account of the Ceylon business. It will thus be seen that if the "seven years" mentioned in clause (a) be taken as seven calendar years, the manager cannot be said to have been in British India during that period for more than two years, and the assessee's joint family would be entitled, under the second proviso to Section 4 (1) as a person "not ordinarily resident" in British India, to claim the exclusion of the foreign income from the assessment. The claim was accepted by the Tribunal and the assessment was ordered accordingly to be reduced. The Commissioner of Income-tax having challenged the correctness of

that view, the Tribunal has referred the following question to this Court for its decision :—

"Whether, in the circumstances of the case, in computing the period or periods when the manager of the Hindu undivided family had not been in British India, the 'seven years' in Section 4-B of the Income-tax Act should be taken as seven calendar years or seven previous years."

It may be mentioned here that the assessee raised before the Tribunal an alternative contention, *viz.*, that even if the aggregate period of the manager's stay in British India during the relevant years be taken as 731 days, it cannot be said to be "more than two years" as the seven years, however reckoned, must include at least one leap year. But the Tribunal did not decide the point and it is not before us.

It is necessary, in order to appreciate the contentions of the parties, to describe in brief outline the scheme of taxation laid down in the Act so far as it is material here. The tax is levied for each financial year commencing on the 1st of April at the rate or rates prescribed in the Finance Act in force for the time being and is charged on the "total income of the previous year" (Section 3). The "previous year" may be either the financial year next preceding or, at the option of the assessee, any other period of twelve months ending within such year if he has made up his accounts for such period. It was held that an assessee could not have two separate "previous years" for the purpose of income-tax (*Commissioner of Income-tax, Bombay* v. *Abubaker Abdul Rahman*[1]) but this view was superseded by the amending Act, and it is now possible for an assessee to have a different "previous year" for each separate source of income [Section 2 (11)]. "Total income" is the total amount of income, profits and gains referred to in sub-section (1) of Section 4 computed in the manner laid down in the Act [Section 2 (15)]. Section 4 (1) refers to four classes of income and provides for their assessment on a basis which differs according as the assessee is or is not "resident" or "ordinarily resident" in British India *during the previous year* of which the income falls to be assessed. It is, accordingly, with reference to that year, that the various tests of "residence" or "ordinary residence" as defined in Section 4-A and Section 4-B have to be applied. The question is whether the "seven years preceding the year" mentioned in Section 4-B (a) refers to the seven years ending on that day next preceding the commencement of the previous year or to the period of seven years ending on the 31st December preceding the commencement of such year as suggested for the assessee.

Mr. P. R. Srinivasan appearing for the assessee relies on Section 3 (59) of the General Clauses Act (X of 1897) which provides that in

(1) (1936) 4 I.T.R. 233; I.L.R. 60 Bom. 679.

all Central Acts and Regulations made after the commencement of that Act, unless there is anything repugnant in the subject or context, "year" shall mean "a year reckoned according to the British calendar." As the Calendar (New Style) Act, 1750, (24 Geo. 2, C. 23) transferred the beginning of the year in England from 25th of March to 1st of January in and after 1752, it is urged that, in applying Section 4-B (a), the seven years must be reckoned commencing from the 31st December preceding the year of account and counting backward. We cannot agree. It is obvious that this mode of computation would result in a gap, an interregnum, before the commencement of the "previous year" except, of course, where that year also began from the 1st of January. Such a result is repugnant to the intendment of the provisions of Section 4-B (a) read with Section 4 (1) under which the *terminus ad quem* is the commencement of the "previous year." We find nothing in Section 50 of the Act to which reference was made in the course of the argument to support the interpretation contended for on behalf of the assessee.

It was said that if the "seven years" mentioned in Section 4-B (a) were taken as referring to the period immediately preceding the year of account, it would give rise to the anomalous position of one and the same person being liable to assessment as "resident" in respect of some of his sources of income and as "not resident" in respect of others according to the "previous year" he has adopted for the respective sources. This argument appears to have weighed very much with the Tribunal, but we see no force in it. It is true, as has been stated, that under Section 2 (11) as amended, it is possible for an assessee to have as many "previous years" as he has separate sources of income. But, as we have pointed out already, under the scheme of taxation laid down in the Act the charge is made on the total income of the "previous year," and such income has to be computed on the basis of the assessee's residence or non-residence in British India during that year. That is to say, in respect of *each* separate source of income the year of account is to be ascertained, and if it is found on applying the provisions of Sections 4-A and 4-B with reference to *that year* that the assessee was "resident" or "not resident" or "not ordinarily resident" in British India as the case may be, the income of *that year* is to be computed on the appropriate basis indicated and the total of the amounts thus computed for all the sources of income, whether British Indian or foreign, is to be charged to tax. Such procedure may prove somewhat cumbrous but not unworkable in its application to particular cases where the assessee has adopted different years of account for his separate sources of income and it is possible in such cases that he should be assessed as resident in

respect of some of the sources and non-resident in respect of others. But this, in our opinion, is no reason for disregarding a construction to which the language of the provisions in question plainly points. And, after all, the construction contended for on behalf of the assessee, as we understand it, does not help to resolve the supposed anomaly as, even on such construction, an assessee may, in conceivable cases, have to be dealt with as resident and non-resident in respect of his different sources of income.

We are therefore of opinion that the expression "seven years" in Section 4-B of the Indian Income-tax Act should be taken as referring to the period of seven years of twelve calendar months each immediately preceding the commencement of the relevant previous year, and we answer the reference in that sense. The assessee will pay Rs. 250/- as costs of the Commissioner of Income-tax.

Reference answered accordingly.

[IN THE NAGPUR HIGH COURT.]

INCOME-TAX APPELLATE TRIBUNAL, BOMBAY

v.

BACHRAJ NATHANI OF RAIPUR.

GRILLE, C. J., and NIYOGI, J.

April 4, 1945.

INDIAN INCOME-TAX ACT (XI OF 1922), SEC. 25 (3)—EXCESS PROFITS TAX ACT (XV OF 1940), SEC. 2 (21)—"DISCONTINUANCE"—PARTNERSHIP CARRYING ON BUSINESS IN SEVERAL BRANCHES—DISSOLUTION—BRANCHES TAKEN OVER AS GOING CONCERN BY QUONDAM PARTNERS—WHETHER DISCONTINUANCE OF BUSINESS—RIGHT TO RELIEF UNDER SEC. 25 (3).

Two divided Hindu brothers carrying on business in partnership with a head office and several branches agreed on December 31, 1938, to dissolve the partnership and nominated an arbitrator to divide the business assets and liabilities into moieties by means of two awards. From January 1, 1939, each of the brothers as manager of his family consisting of himself and his sons carried on business under different trade names. The actual division was made by the arbitrator by means of two awards dated March 15 and October 11, 1939. The Income-tax Appellate Tribunal found that each of the shops was taken over by one or other of the brothers as a going concern together with its books and the profits of the firm were not capitalised or distributed at the time of its dissolution nor were the books balanced. Each of the brothers in substance continued the moiety of the business that fell to his share instead of carrying on the business jointly as before the division:

Held, (*i*) *that there was no discontinuance of business in spite of the dissolution of partnership and no relief under Section 25 (3) of the Income-tax Act could be granted;*

(*ii*) *that there could be no commencement of any business as such after July 1, 1938, so as to attract the application of the 2nd proviso to Section 2 (21) of the Excess Profits Tax Act.*

When a unit of business devolves on an heir or is sold to a purchaser, there is a clear case of succession because there is nothing but a change of ownership. In such a case, neither the identity nor the integrity of the business is impaired. But difficulty arises in the case of division of a business which is run in several branches which are carried on independently but which attain apparent unity only by reason of common ownership. When there is a division of such a running business and the quondam partners become the exclusive owners of the branches of the parent business, the fact that because of partition of the original business the branches lose their organic relation with each other does not necessarily imply the discontinuance of the business of the branch which passes into the hands of the quondam partner. To be able to say that with respect to the branch that the business has ceased, the parent business must have terminated so that the branch which becomes independent should cease to be going concern when it passes into the hands of the quondam partner. The business in his hands would, if it was running independently even though as a factor of a larger unit, change its identity or integrity.

Cases referred to :—

Commissioner of Income-tax, Madras *v.* Best and Co., Madras [1932] (55 Mad. 832; 138 I.C. 485; A.I.R. 1932 Mad. 434; 63 M.L.J. 15; 6 I.T.C. 92).

Commissioner of Income-tax *v.* A.L.V.R.P. Firm [1940] (8 I.T.R. 531; A.I.R. 1940, Rang. 281; 192 I.C. 561)

Commissioner of Income-tax, Burma *v.* N.N Firm [1934] (2 I.T.R. 85; 148 I.C. 594; A.I.R. 1934 Rang. 13; 11 Rang. 501; 7 I.T.C. 55)

Commissioner of Income-tax, Madras *v.* Karuppiah [1941] (I.L.R. 1941 Mad 220; 194 I.C. 118; A.I.R 1941 Mad. 255.; 9 I.T.R. 1).

Commissioner of Income-tax, Burma *v.* Mansookhlal Zaveri [1937] (5 I.T.R. 664; 168 I.C. 209; A.I.R. 1937 Rang. 102; I.L.R. 1937 Rang. 26; 10 I.T.C. 198)

Commissioner of Income-tax, Bombay *v.* Sanjana & Co., Ltd. [1926] (50 Bom. 87; 92 I.C. 517; A.I.R. 1926 Bom. 129; 27 Bom. L.R. 1471; 2 I.T.C. 110).

Hanutram Bhuramal *v.* Commissioner of Income-tax, Bihar and Orissa [1938] (6 I.T.R. 290).

Kalu Mal *v.* Commissioner of Income-tax, Punjab [1929] (A.I.R. 1929 Lah. 461; 117 I.C. 229; 3 I.T.C. 341).

M. Kannappa Naicker & Co. *v.* Commissioner of Income-tax, Madras [1937] (5 I.T.R. 49; 168 I.C. 13; A.I.R. 1937 Mad. 316; (1937) 1 M.L J. 619; I.L.R. 1937 Mad. 814; 10 I.T.C. 154).

Michael Faraday *v.* Carter [1927] (11 Tax Cas. 565).

Ram Rakha Mal *v.* Commissioner of Income-tax [1937] (5 I.T.R. 137; A.I.R. 1937 Lah. 830; 172 I.C. 821; I.L.R. 1937 Lah. 325).

Wilson and Barlow *v.* Chibbett [1929] (14 Tax Cas. 407).

Reference by the Income-tax Appellate Tribunal, Bombay: Miscellaneous Civil Case No. 46 of 1944.

STATEMENT OF CASE.

" These are seven connected applications requiring the Tribunal to refer certain questions of law to the Nagpur High Court under Section 66 (1) of the Indian Income-tax Act and Section 21 of the Excess Profits Tax Act read with Section 66 (1) of the Income-tax Act.

2. The applications, which are numbered 66 R.A. Nos. 6 to 11 and 13 (C.P.) of 1943-44, relate to the Tribunal's orders in 14 (1) E.P.T.A.A. Nos. 10, 8, 7 and 9 (C.P.) of 1942-43 and R.A. Nos. 45 and 44 (C.P.) of 1941-42 and No. 12 (C.P.) of 1943-44 respectively.

3. For the purpose of these applications it is only necessary to briefly state the following facts. Seth Balkishan and Seth Ramkishan, two divided Hindu brothers, were carrying on a business in partnership under the style of Seth Balkishan Ramkishan Nathani with its head office at Raipur and several branches at other places, up to the 31st December 1938, when the partners agreed to dissolve the partnership. The partnership was accordingly dissolved and the business assets and liabilities of the partnership were divided into two moieties by means of two awards. Thereafter the two brothers carried on their individual businesses similar in nature to the business carried on by the old partnership. In the course of the 1939-40 assessment proceedings a claim was made for relief under Section 25 (3) of the Income-tax Act. The accounting period relating to that assessment was from Dewali 1937 to Dewali 1938, while the alleged discontinuance of the business was claimed to have taken place on 31st December 1938, the date of the dissolution of the old partnership. The matter came up before another Bench of the Tribunal in appeal and was dealt with by the Bombay Bench by its order dated June 9, 1941. It was held therein that "the dissolution of the partnership between the two brothers did not amount to anything more than a division of the properties, business and its assets and liabilities between the two, each taking over a moiety for his share. Each of the shops at Neora and Baloda Bazar was taken over by one or the other of the brothers as a going concern together with its books." In view of this finding of fact the Bench came to the conclusion that there had been no discontinuance of the business, in terms of Section 25 (3) on December 31, 1938. The alternative claim of the appellant for relief under Section 25 (4) was rejected by that order on the ground that the succession had admittedly not taken place on or after the 1st April 1939. Being dissatisfied with the Tribunal's order, the two branches of the family made applications to the Tribunal claiming a reference to the High Court on certain

questions of law alleged to arise from the Tribunal's order. This application was dismissed by the Tribunal, mainly on technical grounds, although in dealing with the reference applications the Bench concerned expressed the opinion that no question of law arose out of their order dated 9th June 1941. The matter rested there.

4. The question, however, cropped up again for the purpose of the 1940-41 income-tax assessments and the excess profits tax assessments since the period from Dewali 1938 up to December 31, 1938, formed part of the accounting period relating to the 1940-41 income-tax assessments and of the chargeable accounting periods for the excess profits tax assessments. The applicants reiterated their claim for relief under Section 25 (3) of the Income-tax Act for the income-tax assessments and claimed the benefit of the second proviso to Section 2 (21) of the Excess Profits Tax Act for the excess profits tax assessments. In view of the Tribunal's finding in R.A.A. Nos. 4, 5 and 6 (C.P.) of 1941-42 relating to the 1939-40 assessment, both the Income-tax *cum* Excess Profits Tax Officer and the Appellate Assistant Commissioner dismissed the applicants' claim.

5. The four assessments under the Excess Profits Tax Act and the three assessments under the Income-tax Act came upon appeal before this Bench of the Tribunal. No fresh facts were brought to our notice, but the contentions raised in connection with the 1939-40 appeals were urged for a second time. This Bench of the Tribunal saw no reason to differ from the findings arrived at in R.A.A. Nos. 4, 5 and 6 (C.P.) of 1941-42 and held that there had been no discontinuance of the business formerly styled as Seth Balkishan Ramkishan Nathani, within the meaning of Section 25 (3) of the Income-tax Act. In view of ths Tribunal's finding that there had been no discontinuance of the business of 31st December 1938 and no new business had been started on 1st January 1939, it followed that the business of the assessee did not commence after the 1st day of July 1938, and the Tribunal therefore held that the assessee was not entitled to the benefit of the second proviso to Section 2 (21) of the Excess Profits Tax Act and rejected the applicants' claim. These applications arise out of the Tribunal's orders dismissing the appeals.

6. The respondent in his reply under rules 53 and 54 of the Appellate Tribunal Rules contends that no question of law arises out of the orders of the Tribunal. We are, however, of the opinion that the following question of law arises out of our orders, which we accordingly refer to the High Court of Judicature at Nagpur :—

'Whether on the findings arrived at by the Appellate Tribunal in their order dated June 9, 1941, the legal inference is one of discontinuance of business within the meaning of Section 25 (3) of the Indian Income-tax Act?'

7. Our first reaction to the applications relating to the excess profits tax assessments was that the point involved was a pure finding of fact. The Tribunal found that the businesses of the assessees were not commenced after the 1st day of July 1938 and the benefit of the second proviso to Section 2 (21) of the Excess Profits Tax Act was not therefore available to the assessees. This finding, however, was a necessary consequence of the finding that there had been no discontinuance of the business on 31st December 1938, within the meaning of Section 25 (3) of the Income-tax Act. Since the basic finding has been treated by us as being a mixed question of fact and law, the ultimate decision in the excess profits tax appeals must turn upon the answer to the question referred by us to the High Court in connection with the income-tax assessment appeals. It is not, therefore, necessary for us to formulate any separate question in respect of the excess profits tax assessments."

R. Kaushalendra Rao, for the Commissioner.

R. N. Padhye, for the assessee.

JUDGMENT.

This case and Miscellaneous Civil Cases Nos. 81 and 82 of 1944 arise out of reference made by the Income-tax Appellate Tribunal, Bombay, under Section 66 (1) of the Indian Income-tax Act and Section 21 of the Excess Profits Tax Act read with Section 66 (1) of the Income-tax Act; and Miscellaneous Civil Cases Nos. 5, 6 and 7 of 1942 are applications made by the assessees under Section 66 (2) of the Income-tax Act. The issue common to all these cases is embodied in the following question formulated by the Tribunal:—

"Whether on the findings arrived at by the Appellate Tribunal in their order dated June 9, 1941, the legal inference is one of discontinuance of business within the meaning of Section 25 (3) of the Income-tax Act?"

This order governs the disposal of all the cases.

The facts are that Seth Balkishan and Seth Ramkishan, two divided Hindu brothers carried on business in partnership under the style of Seth Balkishan Ramkishan Nathani with its head office at Raipur and several branches at other places. On December 31, 1938, the partners agreed to dissolve the partnership and nominated an arbitrator to divide the business assets and liabilities of the partnership into moieties by means of two awards. From January 1, 1939, Ramkishan as manager of the family consisting of himself and his sons carried on business under the style of Ramkishan Shaligram Nathani, and Balkishan and his sons under the style of Shaligram Laxmichand.

The actual division was made by the arbitrator by means of 2 awards dated March 15, and October 11, 1939. The first made an equal division of the bulk of the properties and business assets. The whole of the business was divided into two lots, one lot being picked up by each, except that the stock of cloth in Raipur shop and the paper agency were made over to Seth Ramkishan at a valuation. A similar division of the business was made of the Bhatapara shop. The business at Neora was allotted to Seth Ramkishan together with its books while Baloda Bazar was made over to Balkishan. In the former, Seth Balkishan took over the shop's debtors to the extent of Rs. 1,478, while in the latter, the other brother took over a similar outstanding to the extent of Rs. 2,705. The firm's interests in several other concerns were made over to one or the other. The second award divided the only two remaining shops, Bhavani Patna and Nandgaon. Seth Ramkishan died on May 28, 1939, after the first division of the bulk of the properties and assets and the managership of his family devolved on his son Bachraj.

At the time of assessment for the year 1939-40, Seth Balkishan and Seth Bachraj, along with other brothers of the family, made a joint application on December 12, 1939, to the Income-tax Officer stating that the firm of Seth Balkishan Ramkishan Nathani discontinued its business from the date of its dissolution and that the two brothers began carrying on the business that fell to their respective shares separately. On that ground they claimed the benefit of Section 25 (3) of the Income-tax Act contending that they were not liable to pay income-tax from the Dewali of 1938 to December 31, 1938. In the alternative, the applicants claimed an exemption from payment of the tax for the period under Section 25 (4) of the Act alleging that at all events, Seth Balkishan and Seth Ramkishan had each succeeded to the old firm. This branch of the claim was rejected by the Income-tax Officer with the remark that Section 25 (4) expressly excluded from its application a case of succession that had taken place before April 1, 1939. That claim was pressed unsuccessfully before the Assistant Commissioner of Income-tax and eventually abandoned before the Tribunal.

The Tribunal found that each of the shops at Neora and Baloda Bazar was taken over by one or the other of the brothers as a going concern together with its books and admittedly the profits of the firm were not capitalised or distributed at the time of its dissolution, nor were the books balanced. Each of the brothers in substance continued the moiety of the business that fell to his share instead of carrying on the business jointly as before the division. The Tribunal held that the dissolution of partnership between the two brothers did not amount to

anything more than a division of the properties, business and its assets and liabilities between the two, each taking over a moiety of his share. The Tribunal was of opinion that the only change effected was a change in the proprietorship of the old business and that it did not amount to a discontinuance of business within the meaning of Section 25 (3) of the Income-tax Act. On these grounds, the Tribunal dismissed the assessees' application by an order dated June 9, 1941. The assessees applied to the Tribunal claiming a reference to the High Court, but that application was dismissed on the ground that no question of law was involved. Thereupon the assessees filed 3 applications under Section 66 (2) of the Income-tax Act for requiring the Tribunal, Bombay, to state the case and refer it to this Court.

The question came up again in the course of the Income-tax assessment of the year 1940-41 and the excess profits tax assessment for the period between the Dewali 1938 and December 31, 1938. The assessees reiterated their claim under Section 25 (3) of the Income-tax Act and claimed the benefit of the second proviso to Section 2 (21) of the Excess Profits Tax Act. But their claim was rejected by the Income-tax *cum* Excess Profits Tax Officer and the Assistant Commissioner of Income-tax. The assessees took their appeals against the four assessments under the Excess Profits Tax Act and three assessments under the Income-tax Act before the Tribunal. No fresh facts were brought to the notice of the Tribunal, but the assessees urged for the second time their old contention that there was discontinuance of the business of the firm styled as Seth Balkishan Ramkishan Nathani within the meaning of Section 25 (3) of the Income-tax Act. That contention was rejected as the result of the Tribunal's finding that there had been no discontinuance of business on December 31, 1938, and that no new business had been started on January 1, 1939. And inasmuch as, in view of the previous finding, the business of the assessees could not be said to have commenced after July 1, 1938, the Tribunal held that the assessee was not entitled to the benefit of second proviso to Section 2 (21) of the Excess Profits Tax Act and rejected the assessee's claim. Nevertheless the Tribunal took the view that its finding that there was no discontinuance of business within the meaning of Section 25 (3) of the Indian Income-tax Act, was a legal inference from the facts found and referred the question reproduced above for our decision.

The case, as presented on behalf of the assessees is that it is either one of succession or discontinuance of business. If it is not one of succession, it must follow as a corollary that it is one of discontinuance of business. This argument is rested on the undermentioned clause occurring in sub-section (3) of Section 25 of the Income-tax Act :

"Where any business.........is discontinued, then, unless there has been a succession by virtue of which the provisions of sub-section (4) have been rendered applicable, no tax shall be payable........."

Reliance is also placed on *Commissioner of Income-tax, Burma* v. *N. N. Firm*[1], *Commissioner of Income-tax, Burma* v. *S. Mansookhlal Zaveri*[2], *Commissioner of Income-tax, Burma* v. *A. L. V. R. P. Firm*[3], *M. Kannappa Naicker & Co.* v. *Commissioner of Income-tax, Madras*[4], *Commissioner of Income-tax, Madras* v. *Best & Co., Madras*[5], *Hanutram Bhuramal* v. *Commissioner of Income-tax, Bihar*[6] and *Wilson and Barlow* v. *Chibbett*[7]. These cases mostly deal with cases of succession falling under Section 26 (2) of the Income-tax Act although they indirectly go to indicate the circumstances in which a business may be regarded as discontinued. These cases and others cited by the other side will now be examined.

In *Commissioner of Income-tax, Burma* v. *N. N. Firm*[1], the facts were that a joint Hindu family consisting of five members which carried on money-lending business decided to partition the family property and referred the partition to arbitration. During the period the arbitration was in progress no fresh loans were advanced. Under the partition, one of the members received 1/5th share of the assets of the money-lending business and the other 4 members carried on the business at the old premises as before the partition. It was held that there was no succession to the money-lending business of the joint family within the meaning of Section 26 (2) of the Income-tax Act on the principle that succession signifies that one person takes the place of another and carries on the business as a whole but that where the business is split up and thereafter another person carries on part of the business, he cannot be said to succeed his predecessor in carrying on the business within the meaning of Section 26 (2). It was also pointed out that where there is no continuity in carrying on the business and when one business has come to an end and after a time another business is started although with the same assets and under the same conditions, the person carrying on the new business cannot be said to succeed to those who had carried on the old business. Now, it must be noticed that there were two branches of the business, one of rice-milling and another of money-lending. The separating member took 1/5th share of the assets of money-lending business and started a business on his own account under a different name and on new premises. As they did not desire that the rice-mill should be sold, they arranged

(1) (1934) 2 I.T.R. 85.
(2) (1937) 5 I.T.R. 664.
(3) (1940) 8 I.T.R. 531.
(4) (1937) 5 I.T.R. 49.
(5) (1932) 55 Mad. 832 ; 6 I.T.C. 92
(6) (1938) 6 I.T.R. 290.
(7) (1929) 14 Tax Cas. 407.

that the separating member's share in it should be bought out by the others. The rice-milling business was continued as before as a whole with this difference that instead of there being five co-owners, there were four and it was held that it was a case of succession. As to the money-lending business which was started by the separated member, it must be observed that the old money-lending business had stopped and therefore, there could not be any succession to a business which was not in existence. The remark made in the judgment that where a business is split up and thereafter another person carried on part of the business, that person does not succeed his predecessor in carrying on the business within Section 26 (2) was obiter in view of the finding that the old money-lending business had ceased. It may be that when a person carries on a part of the old business, he does not succeed but it does not necessarily follow that the old business discontinued if the part is taken over as a going concern. This case was commented upon in *Commissioner of Income-tax, Burma* v. *S. Mansookhlal Zaveri*[1], and it was pointed out that the real test was the identity of the two businesses to determine whether the case would be one of succession or the other. These two cases were followed in *Commissioner of Income-tax, Burma* v. *A. L. V. R. P. Firm*[2]. That was a case of a Hindu joint family which carried on the business of banking and money-lending at Madras and other places including Rangoon and Myitkyo with its head office at Devakottai in the Madras Presidency up to and including the year 1936-37. The income of the family was assessed to income-tax as a Hindu undivided family in Madras. Following upon the separation of Burma from India, the income of the family from Burma was assessed at Rangoon for the year 1937-38. But in 1938-39 when the assessment came to be made, it transpired that the undivided family had partitioned, and as a result of the partition, two brothers, P and V, carried on the Rangoon business as a contractual partnership while V carried on the Myitkyo business alone. The contractual partnership claimed the benefit of the provisions of Section 25 (3) of the Income-tax Act but the Assistant Commissioner held that though the businesses at Rangoon and Myitkyo were separate, the latter was so small that the Rangoon business was substantially the whole business and therefore, there could be a succession to the Rangoon business alone. It is not clear from the judgment whether the learned Judges found that the contractual partnership was a new business or continuation of the old business. To determine whether it was a case of succession it was necessary to find whether the business in Burma was regarded as a separate business

(1) (1937) 5 I.T.R. 664. (2) (1940) 8 I.T.R. 531.

by the joint family or as a branch of the joint business. The learned Judges apparently looked at the question from this point of view, namely, that the business in Burma which was a limb of the original joint business with its headquarters at Devakottai must be deemed to have come to an end when it became an independent business in the hands of the contractual partnership of the two brothers, P and V. The rule that can be deduced from this is that when, as a result of a partition of a joint business, a branch of that business goes into the exclusive ownership of one of the quondam joint owners or partners, the old business of the branch must be deemed to have discontinued, because it ceased to be a branch and became a stem itself. In such a case, it may be noted that the business continues exactly as it was before with this difference that instead of the profits of the branch business going into a pool for the benefit of the joint family as a whole, they go to one of the quondam joint owners exclusively. There is a change of ownership or, at any rate, the quantum of ownership over the branch. But does that necessarily mean discontinuance of the business as such?

In *Hanutram Bhuramal* v. *Commissioner of Income-tax, Bihar*[1], it was pointed out that the phrase "discontinuance of business" is apt to be used in an ambiguous sense and that where a business changes hands or a partner ceases to be a partner, there is no discontinuance of business but only a change in the ownership of the business. In this case one member separated and the remaining members, as in the rice-milling business in *Commissioner of Income-tax, Burma* v. *N. N. Firm*[2], continued to carry on the family business. It was held that the business could be regarded as discontinued, that is to say, that succession postulates continuity of business.

In *Kannappa Naicker & Co.* v. *Commissioner of Income-tax, Madras*[3], it was pointed out that there can be succession to business only when the same business is carried on by different person or persons, but that where a business terminates and a different though a similar business is carried on by another person or a newly constituted firm, there is no succession. This is on the same principle as the money-lending business in *Commissioner of Income-tax, Burma* v. *N. N. Firm*[2] though it is not referred to therein. In this case, the manager of a joint Hindu family had been supplying coolies to the Madras Port Trust under a contract entered into from time to time and after his death his sons continued to supply coolies. Two other persons, R and G, as partners were also similarly supplying coolies

(1) (1938) 6 I.T.R. 290.
(2) (1934) 2 I.T.R. 85.
(3) (1937) 5 I.T.R. 49.

to other godowns of the Port Trust. The contract given to these firms expired on August 31, 1933, and the Port Trust decided to call for tenders for a contract for 5 years. The members of the joint family and R and G joined in making a common tender and agreed to share profit and loss in certain proportions. Their tender was accepted and they formed themselves into a new firm and supplied coolies from September 1933. No assets or liabilities of the joint family or the partners R and G passed to the new firm but the business was carried on under the name under which the joint family had previously carried on the business in their old premises with most of the old employees being taken over. The question was whether the new firm was liable to be assessed under Section 26 (2) of the Income-tax Act as a successor in the business to the previous joint family and the partners R and G, and it was held that they were not successors to the old business as it was not the same business, though similar in nature. The obvious reason was that the old business, depending as it did on the contract which expired on August 31, 1933, had terminated with that contract.

The case reported in *Commissioner of Income-tax, Madras* v. *Best and Co., Madras*[1], was distinguished on the ground that one of the branches of the business, which Messrs. Best and Co. sold as a going concern to a new company, involved the succession of the new company as the business was identical. It may be pertinent to notice that in *Commissioner of Income-tax, Madras* v. *Best and Co., Madras*[1], Best and Co. owned and controlled several companies including Eagle Rolling Mills which they transferred to a new company. The Income-tax authorities assessed the new company under Section 26 (2) of the Income-tax Act holding that the new company succeeded Best and Co. as Eagle Rolling Mills. The assessee company's contention was that it was not a successor to the business of Messrs. Best and Co. because it did not succeed to all the business which Messrs. Best and Co. owned and controlled. The argument was put forward on the assumption that the expression "any business" in Section 26 meant "each and every business." That contention was thrown out and it was held that the new company was the successor of Best and Co. in respect of the Eagle Rolling Mills and that they were liable to be assessed under Section 26 (2). This case is not reconcilable with *Commissioner of Income-tax, Burma* v. *A. L. V. R. P. Firm*[2], where it was held that where a branch ceases to be a branch but becomes a stem, the business of the branch must be deemed to have been discontinued. In this case, the Eagle Rolling Mills though it had

(1) (1932) 55 Mad. 832. (2) (1940) 8 I.T.R. 531.

ceased to be branch, was held not to have discontinued. The facts that in the Rangoon case the branch passed into the exclusive ownership of the quondam members of the joint family and that in the Madras case it passed into stranger's hand does not appear to be material so far as the question of continuance and discontinuance of the business is concerned.

In *Wilson and Barlow* v. *Chibbett*[1], the old company went into liquidation and the new company purchased its lands and property and stock-in-trade. The new company retained the old company's employees and continued without any interruption the work in the old company's premises but did not take over the liabilities of the liquidated concern. It was held that though the new business was the same as the old one, it could not be regarded as identical because it was not the case of a business running on and a new person becoming interested as owner. In *Commissioner of Income-tax, Bombay* v. *Sanjana & Co., Ltd.*[2], on the other hand, it was held that where one company goes into voluntary liquidation and its business is transferred to, and continued by a new company, the liquidators of the old company were not entitled to any refund for the reason that the old business had not been discontinued but only passed to the new company. It was pointed out that the transfer of ownership left the business wholly unaffected.

In *Kalu Mal* v. *Commissioner of Income-tax, Punjab*[3], a joint family consisting of a father and six sons became divided, the sons separated and started business of their own and the father retained the old business with all the rights appertaining thereto. The father's contention was that the old business, as a consequence of disruption in the family, had discontinued within the purview of Section 25 (3) but the Income-tax authorities held that the father only succeeded to what was formerly a joint family business. The question whether the business discontinued or not in consequence of the breaking up of a family was treated as a question of fact to be determined according to the facts of each case and the view of the Income-tax authorities was accepted. In *Commissioner of Income-tax, Madras* v. *Karuppiah*[4], there was a partnership of V and K; V retired from the partnership receiving a sum in lieu of his share of profits, the other partner K carried on the business for his own benefit: it was held that K succeeded to the business of the partnership after dissolution on the principle that a firm as an entity was quite different from the partners who composed it. It was argued that the old partnership business should be

(1) (1929) 14 Tax Cas. 407.
(2) (1926) 50 Bom. 87; 2 I.T.C. 110.
(3) (1929) A.I.R. 1929 Lah. 461; 3 I.T.C. 341.
(4) (1941) 9 I.T.R. 1.

deemed to have been discontinued but that argument was repelled on the ground that when the business of the quondam partnership is carried on without any break by one of the partners after dissolution, the section that is applicable is Section 26 (2) and not Section 44 of the Indian Income-tax Act.

In *Michael Faraday* v. *Carter* [1], A and B, partners, had dissolved their partnership by a deed dated November 22, 1922, as from April 1, 1922. Upon dissolution of the partnership, A continued to carry on business at the firm's address but from November 22, 1922, until his death on July 17, 1923, B carried on in his own name a small amount of business previously done by the firm. By a deed dated December 15, 1922, A took C into partnership as from April 1, 1922. It was held that there has been no discontinuance but that A had succeeded to the business of A and B, and that A and C succeeded to the business carried on by A after the dissolution of his partnership with B. The decision turned on the issue of fact whether the business was identical or not and the finding was that the business was one business all through as it never lost its identity.

On a review of the authorities, it would appear that the question, whether there is succession or discontinuity of business, was treated as a mixed question of law and fact but the actual decision eventually turned on the particular facts of each case. The rule which can be broadly deduced from them is that succession postulates continuity of the business as a whole so that it retains its identity despite the change of partnership, but the cases do not make it clear whether integrity and identity of business are the essential elements of the continuity of the business. When a unit of business devolves on an heir or is sold to a purchaser, there is a clear case of succession because there is nothing but a change of ownership. In such a case, neither the identity nor the integrity of the business is impaired. Such a simple case would no doubt be a good illustration of the rule. But difficulty arises in its application to a case of division of a business which is run in several branches which are carried on independently but which attain apparent unity only because of common ownership. When there is a division of such a running business and the quondam partners become the exclusive owners of the branches of the original business, can it not be predicated that it is a case of succession for the reason that the original business of the branch continues as before? The fact that as a result of partition of the parent business, the branches lose their organic relation with each other does not necessarily imply the discontinuance of the business of the branch which passes into the hands of the quondam partner. To be able to say

(1) (1927) 11 Tax Cas. 565.

that with respect to the branch that the business has ceased, the parent business must terminate so that the branch which becomes independent should cease to be going concern when it passes into the hands of the quondam partner. The business in his hands would, if it was running independently even though as a factor of a larger unit, change its identity or integrity. To elucidate the principle, let us take two illustrations: (1) A and B jointly carry on business consisting of 4 branches. They effect partition in such a way that 2 branches go to one and 2 to another, all the branches being active at the time of the division. This would be a case of succession because there is no change in the business but only in the ownership. Each of the branches retains its integrity as well as identity. (2) A and B jointly carry on only one running business, *e.g.*, a shop. They divide the shop with the result that each of them gets ½ of the shop as a going concern. Here it may be said that the business has lost its integrity and perhaps also its identity but can it be said that it has discontinued? This conceivably represents a case on the border line of continuity and discontinuity of business. Now supposing that A and B run a joint business with 9 branches. They divide the business in such a way that 4 branches go to each of them and one branch is divided into 2 moieties. In such a case, the business which falls to the share of each may well be regarded as whole and identical in spite of the fact that they include a fraction of an old branch as was done in *Commissioner of Income-tax, Burma* v. *A. L. V. R. P. Firm* [1] in the case of Myitkyo business. As so regarded, the conclusion would be a conclusion of fact.

We will now proceed to examine the argument that as the assessee's case is not a case of succession, it must be a case of discontinuity of business. This argument rests on an imperfect application of the meaning of the words " then unless " in sub-section (3) of Section 25. On their true construction, they mean " except when." It must be observed that sub-section (3) is concerned with business, profession or vocation and sub-section (4) with person. When an owner of a business dies or transfers his business or when partners dissolve their partnership, there is discontinuance so far as the person dying or transferring or the separating partners are concerned but there may be no discontinuance of the business as such. Thus the word discontinuity is capable of a double interpretation according as it is *vis-a-vis* the owners or *vis-a-vis* the business. In the former case, the discontinuity is notional or jural and in the latter case, it is real or factual. The word " unless " occurring in sub-section (3) is used to exclude the case of notional or jural discontinuity from the purview of that

(1) (1940) 8 I.T.R. 531.

sub-section because it is, in reality, a case of succession postulating continuity of business as opposed to discontinuity in truth and in fact. Consequently, it indicates that, being an exception to the discontinuity contemplated in sub-section (3), it should be dealt with under sub-section (4). The word succession means and includes fractional or partial succession as illustrated in para. 15 above (see *Ram Rakha Mal* v. *Commissioner of Income-tax* [1]) if the business is carried on as it had been done before partition or dissolution of partnership. Succession, therefore, denotes a change in ownership. Consequently, the form which the issue assumes in such cases is whether the business was discontinued, not whether it was discontinued by joint owners.

In the present case, the assessees had perhaps a good case under Section 26 (2) of the Income-tax Act but they could not derive any benefit from it as sub-section (4) of Section 25 excluded a case of succession that has taken place before April 1, 1939. Having been denied the benefit of that section, the assessees had no alternative but to take the position which has become untenable in view of the Tribunal's finding that the business never came to a standstill but was active throughout; the profits of the firm were never capitalised or distributed, each of the businesses was allowed to continue and there was no interruption in the flow of the business as a whole. The Tribunal was right in drawing the inference that there was no discontinuance of business in spite of the dissolution of partnership. Mere division of business does not necessarily signify termination of the business. In our opinion, the Tribunal was right in rejecting the assessees' claim made under Section 25 (3) of the Indian Income-tax Act. On that footing, there could be no commencement of any business as such after July 1, 1938, so as to attract the application of the 2nd proviso to Section 2 (21) of the Excess Profits Tax Act. We answer the reference accordingly. The assessees' applications made under Section 66 (2) of the Income-tax Act are dismissed. The assessees will pay the costs of the references and bear their own. Counsel's fees as certified.

Reference answered accordingly.

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(1) (1937) 5 I.T.R. 137.

[IN THE NAGPUR HIGH COURT.]

INCOME-TAX APPELLATE TRIBUNAL, BOMBAY

v.

CHHAGANMAL MANGILAL.

GRILLE, C. J., and SEN, J. December 8, 1944.

INDIAN INCOME-TAX ACT (XI OF 1922 AS AMENDED IN 1939), SEC. 10 (2) (xii)—BUSINESS EXPENDITURE—LITIGATION EXPENSES—SUIT FOR INFRINGEMENT OF TRADE MARK COMPROMISED—LITIGATION EXPENSES INCURRED IN DEFENDING SUIT AND COSTS PAID TO OPPOSITE PARTY UNDER COMPROMISE—WHETHER ALLOWABLE DEDUCTION.

The assessee carrying on business in cloth started using a certain trade mark on the cloth which he had been selling. A mill filed a suit against the assessee for injunction, rendition of account and damages on the allegation that he had infringed their trade mark and that his trade mark was a colourable imitation of their trade mark. Subsequently the parties compromised the subject-matter of the suit. The assessee incurred an expense of Rs. 3,351, out of which Rs. 1,351 was his own expense in defending the suit and in filing and conducting the appeal and the balance of Rs. 2,000 was the costs of the opposite party paid by him in accordance with the terms of the compromise :

Held, *that the expenditure of Rs. 3,351 was not in the nature of capital expenditure but was a revenue expenditure and as such was an allowable deduction in computing the taxable income of the assessee under Section 10 (2) (xii) of the Indian Income-tax Act.*

Commissioner of Income-tax, Burma v. *Gasper & Co., Rangoon [1940] (8 I.T.R. 100)* doubted*; Amrita Bazar Patrika Co., Ltd., In re [1937] (5 I.T.R. 648 ; A.I.R. 1938 Cal. 241)* distinguished*; Income-tax Appellate Tribunal, New Delhi* v. *Empress Mills, Nagpur [1943] (I.L.R. 1943 Nag. 307 ; 11 I.T.R. 266)* followed.

Cases referred to:

Amrita Bazar Patrika Co., Ltd., *In re* [1937] (5 I.T.R. 648; A.I.R. 1938 Cal. 241; 174 I.C. 817).

Anglo Persian Oil Co. *v.* Dale ([1932] 1 K.B. 124 ; 100 L.J.K.B. 504 ; 145 L.T. 529 ; 47 T.L.R. 487).

British Insulated and Helsby Cables *v.* Atherton ([1926] A.C. 205 ; 95 L.J.K.B. 336; 134 L.T. 289 ; 10 Tax Cas. 155).

Commissioner of Income-tax, Burma *v.* Gasper and Co., Rangoon [1940] (8 I.T.R. 100 ; A.I.R. 1940 Rang. 195 ; 190 I.C. 286 ; 1940 Rang. L.R. 408).

Commissioner of Income-tax, Bihar and Orissa *v.* Kameshwar Singh [1940] (8 I.T.R. 52 ; A.I.R. 1941 Pat. 197 ; 196 I.C. 656).

Commissioner of Income-tax, Bihar and Orissa *v.* Kameshwar Singh [1942] (69 I.A. 15 ; 199 I.C. 314 ; A.I.R. 1942 P.C. 11 ; 23 Pat. 491 ; 10 I.T.R. 214).

Commissioner of Income-tax, C. P. *v.* Mathuradas Mannalal [1942] (10 I.T.R. 95).

Commissioners of Inland Revenue *v.* Alexander Von Glehn & Co., Ltd., ([1920] 2 K.B. 553 ; 89 L.J.K.B. 590 ; 123 L.T. 338 ; 12 Tax Cas. 232).

Commissioners of Inland Revenue *v.* E. C. Warnes & Co., Ltd. ([1919] 2 K.B. 444 ; 89 L.J.K.B. 6 ; 121 L.T. 125 ; 12 Tax Cas. 227).

Income-tax Appellate Tribunal, New Delhi *v.* Empress Mills, Nagpur [1943] (11 I.T.R. 266 ; A.I.R. 1943 Nag. 219 ; I.L.R. 1943 Nag. 307 ; 208 I.C. 280).

Kamakshya Narain Singh *v.* Commissioner of Income-tax, Bihar and Orissa [1943] (A.I.R. 1943 P.C. 153 ; 22 Pat. 713 ; 70 I.A. 180 ; 210 I.C. 1 ; 11 I.T.R. 513).

Kangra Valley Slate Co., Ltd. *v.* Commissioner of Income-tax, Punjab [1935] (3 I.T.R. 324 ; 16 Lah. 479 ; A.I.R. 1936 Lah. 350 ; 161 I.C. 965 ; 7 I.T.C. 375).

Mitchell *v.* B. W. Noble Ltd. ([1927] 1 K.B. 719 ; 96 L.J.K.B. 484 ; 137 L.T. 33 ; 11 Tax Cas. 372).

Scammell & Nephew Ltd. *v.* Rowles ([1939] 1 All E.R. 337 ; 8 I.T.R. Suppl. 41 ; 22 Tax Cas. 479).

Southern *v.* Borax Consolidated Ltd. ([1941] 1 K.B. 111 ; 110 L.J.K.B. 705 ; 23 Tax Cas. 597 ; [1940] 4 All E. R. 412 ; 10 I.T.R. Suppl. 1).

Strong & Co., Ltd. *v.* Woodifield ([1906] A.C. 448 ; 75 L.J.K.B. 864; 95 L.T. 241).

Tushar Kanti Ghosh, *In re* [1935] (A.I.R. 1935 Cal 419 ; 63 Cal. 217 ; 156 I.C. 1055).

Vallambrosa Rubber Co., Ltd. *v.* Farmer [1910] (5 Tax Cas. 529).

Reference under Section 66 (1) of the Indian Income-tax Act, 1922, by the Income-tax Appellate Tribunal, Bombay : Miscellaneous Civil Case No. 52 of 1943.

STATEMENT OF CASE.

" The assessee, Seth Chhaganmal Mangilal, has made these two applications under Section 66 (1) of the Indian Income-tax (Amendment) Act, 1939, inviting us to refer certain questions stated to be questions of law arising out of our appellate judgment in his two appeals R. A. A. Nos. 19 and 20 (C. P.) of 1942-43. The Commissioner of Income-tax, C. P. and U. P., has filed written answers to each of the applications. The two applications and the corresponding answers are marked A and A1, and B and B1, respectively, in the appended list of documents.

2. One of the two questions involved in these references is common to both and arises out of common facts. We, therefore, propose to make a consolidated reference in both cases.

3. The undisputed facts are stated in para. 2 of our judgment. Being few they may be restated. The assessee who deals in cloth was using a colourable imitation of a trade mark to which R. B. Bansilal Abirchand Spinning and Weaving Mills had exclusive right. In consequence, the Mills brought a suit against the assessee to restrain him from using the mark and for damages and costs. The suit which went up to the High Court in appeal finally ended in a compromise in terms of which the assessee undertook to discontinue the use of the trade-mark in question, and also to pay to the plaintiff Mills a sum of Rs. 2,000 for cost of the suit and appeal. He also incurred an expenditure of Rs. 1,351 on his own account in defending the action. Out of

the total amount he debited a sum of Rs. 949 in the year of account relevant to the assessment of 1940-41, and the balance of Rs. 2,402 in the year of account following and relevant to the assessment for the year 1941-42, according as the expenditure was actually incurred.

4. In his assessment for 1940-41, the assessee claimed a deduction of Rs. 949 as legal expenses in the computation of his income which the Income-tax Officer allowed on the ground that it was business expense. Later, another officer who succeeded him, and made the assessment for 1941-42, thought that the expenditure was not an admissible deduction. Accordingly, he not only added the amount of Rs. 2,402, but reopened the preceding year's assessment under Section 34 of the Indian Income-tax Act, and made a revised assessment adding back Rs. 949 which had been originally allowed. Copies of the two assessment orders for 1940-41 and 1941-42 are, respectively, marked C, D and E. The Appellate Assistant Commissioner confirmed the re-assessment for 1940-41 and the assessment for 1941-42 on this point. Copies of his orders are respectively F and G.

5. Two of the questions raised in the assessee's appeal to the Tribunal were, first, whether the expense incurred by him in defending the action brought by the R. B. Bansilal Abirchand Mills was an admissible deduction under Section 10 (2) (xii) of the Indian Income-tax (Amendment) Act, 1939, and, secondly, whether his re-assessment for 1940-41 resulting in the adding back of Rs. 949 could be validly made under Section 34 of the Act. We held against the assessee on both these points for reasons recorded in paras. 4 and 5 of our judgment, a copy of which is Ex. H.

6. These two are questions of law. But before proceeding to formulate them for reference, we shall briefly dispose of a third question formulated by the assessee in para. 6 of his application as to whether there was any material before the Tribunal to hold that the assessee was using another's trade-mark. Obviously, the question as formulated implies that the fact was in contest before us. But that is wholly incorrect, inasmuch as it was expressly admitted in the appellant's memo of appeals, and also in the arguments, that he had incurred the expense in defending the claim made against the profits earned by him by the use of the trade-mark. In our opinion, therefore, the question is misconceived. Thus the only two questions that we propose to refer to their Lordships are :—

Questions referred.—(1) Whether, on the facts of this case, the two sums of Rs. 949 and Rs. 2,402 were admissible deductions in the computation of applicant's income for the two charge years 1940-41 and 1941-42, respectively, under Section 10 (2) (xii) of the Indian Income-tax (Amendment) Act, 1939 ?

(2) If the answer to the first question should be in the negative, whether, in the circumstances of this case, the re-assessment made upon the assessee for the charge year 1940-41 by adding back the amount of Rs. 949 was in accordance with the provisions of Section 34 of the Act ?"

D. N. Chaudhuri, for the Commissioner.

R. N. Padhye, for the assessee.

JUDGMENT.

(Judgment of the Court was delivered by Sen, J.)

This is a reference under Section 66 (1) of the Indian Income-tax Act, 1922, made by the Appellate Tribunal, Bombay, at the instance of the assessee Seth Chhaganmal Mangilal of Amraoti. The relevant facts which have led to the present reference are briefly these. The assessee carries on business in cloth at Amraoti. He is not a manufacturer of cloth but gets his articles manufactured at different mills and had recently started using the *Ganpati chhap* on the dhotis and the bleached long cloth which he had been selling. The business prospered and he made increasing yearly profits as is evident from the figures given by him in his application dated 19th October, 1942, to the Tribunal.

R. B. Bansilal Abirchand Spinning and Weaving Mills, Hinganghat, manufacture various kinds of cloth and have been using the *Narsinha chhap* as their trade mark. They filed Civil Suit No. 8-A of 1939 in the Court of the Second Subordinate Judge, First Class, Amraoti, against the assessee on 5th August, 1939, for injunction, rendition of account and damages on the allegation that he had infringed their trade mark and that his trade mark was a colourable imitation of their trade-mark. On 11th October, 1939, the Court passed an order of temporary injunction against him and in favour of the Mills on condition that they furnished security for making good the loss which the assessee might suffer in consequence thereof in the event of the suit being unsuccessful. The assessee filed Miscellaneous Appeal No. 255 of 1939 in the High Court against the order. During the pendency of the appeal, the parties compromised the subject-matter of the suit and filed an application in the High Court on 20th July, 1940, for directing the lower Court to pass a decree in terms of the compromise. The High Court sent the compromise petition to the lower Court in order to enable it to pass a decree in accordance with the terms of the compromise and dismissed the appeal on 24th July, 1940, as compromised. In the paper book the compromise petition or the decree which was passed in Civil Suit No. 8-A of 1939 has not been included.

The assessee gave Rs. 2,000 to the Mills in accordance with the terms of compromise. He incurred an expenditure of Rs. 1,351 in defending the suit and in filing and conducting the appeal. He had thus incurred an expense of Rs. 3,351, of which his own costs were Rs. 1,351 and that of the opposite party Rs. 2,000. The question for decision is whether the assessee is entitled to deduct this amount in determining his profits or gains in his business. For 1940-41 the assessee claimed a deduction of Rs. 949 on account of the expenses incurred by him in Civil Suit No. 8-A of 1939 in the year of accounting. The claim was allowed by the Income-tax Officer in the order dated 22nd January, 1940.

For the subsequent year 1941-42 the assessee claimed a deduction of Rs. 2,402. This amount represented the costs Rs. 402 which he had incurred and Rs. 2,000 which he paid to the Mills under the compromise in the year of accounting. The matter was decided by another Income-tax Officer who by the order dated 3rd September, 1941, disallowed the sum as not a permissible item of deduction and made an assessment for 1941-42 on that basis. By a separate order he re-opened under Section 34 of the Income-tax Act, 1922, the assessment for 1940-41 and added Rs. 949 and made a revised assessment for 1940-41 accordingly. The orders were upheld by the Appellate Assistant Commissioner of Income-tax, Nagpur, in appeal by the orders dated 8th April, 1942. The Appellate Tribunal, Bombay, by the orders dated 21st August, 1942, affirmed the orders passed by the Appellate Assistant Commissioner of Income-tax. The assessee made two applications to the Appellate Tribunal on 19th October, 1942, for reference to the High Court—one relating to the assessment for 1940-41 and the other for 1941-42.

The two questions which have been referred to us by the Appellate Tribunal are: (1) Whether, on the facts of this case, the two sums of Rs. 949 and Rs. 2,402 were admissible deductions in the computation of the applicant's income for the two charge years 1940-41 and 1941-42, respectively under Section 10 (2) (xii) of the Income-tax (Amendment) Act, 1939? (2) If the answer to the first question should be in the negative, whether, in the circumstances of this case, the re-assessment made upon the assessee for the charge year 1940-41 by adding back the amount of Rs. 949 was in accordance with the provisions of Section 34 of the Act? Under Section 10 of the Income-tax Act of 1922, a tax is payable by an assessee under the head "Business" in respect of any profits or gains of any business carried on by him. In computing such profits or gains certain allowances are permitted. One of such permissible allowances was given in clause (ix) which was in these terms :—

" any expenditure (not being in the nature of capital expenditure) incurred solely for the purposes of earning such profits or gains."

The section and its several clauses were amended by the Income-tax (Amendment) Act, VII of 1939. The amended clause was re-numbered as clause (xii) and runs thus: "any expenditure (not being in the nature of capital expenditure or personal expenses of the assessee) laid out or expended wholly and exclusively for the purpose of such business . . ."

The assessments for 1940-41 and 1941-42 were made after the Income-tax (Amendment) Act, VII of 1939, had come into force. The reference is to be decided in accordance with the provisions of the Income-tax Act, 1922, as amended by Act VII of 1939. The present section may be compared with the provisions of the English Income Tax Act, 1918, which are given in Schedule D, Rules 1 and 3 applicable to Cases I and II which deal with tax payable in respect of any trade not contained in any other schedule. Under Rule 1 the tax is chargeable without any other deduction than is by the Act allowed. Rule 3 is in these terms :—

" In computing the amount of the profits or gains to be charged, no sum shall be deducted in respect of—

(a) any disbursements or expenses, not being money wholly and exclusively laid out or expended for the purposes of the trade . . .

*   *   *   *   *

(f) any capital withdrawn from, or any sum employed or intended to be employed as capital in such trade . . ."

The Indian Income-tax Act so far as the clause " allowance of deductions on account of expenditure wholly or exclusively laid out or expended for the purposes of the trade" has been brought in conformity with the English law; the only difference being that in the Indian Act the allowance is given in one clause in positive terms while in the English Act it stands in a negative form and given in two clauses. The Indian Income-tax Act of 1922 is both in its general framework and its particular provisions different from the English Income Tax Acts, so that decisions upon the English Acts are in general of no assistance in construing the Indian Act. But on some fundamental concepts reference may be to some extent usefully made to English decisions, in particular as to the meaning of the word "income": see *Kamakshya Narain Singh* v. *Commissioner of Income-tax, Bihar & Orissa*[1]. Similarly reference may usefully be made to English cases as to the meaning of the expression " capital expenditure." The English Income Tax Act does not contain any express allowance or enumeration of deductions. Under the Act in determining whether a particular item may or may not be deducted

(1) (1943) 11 I.T.R. 513, at p. 521 ; 70 I.A. 180, at p. 188.

from the profits it is necessary first to inquire whether the deduction is expressly prohibited by the Act and then, if it is not so prohibited, to consider whether it is of such a nature that it is proper to be charged against the incomings in a computation of the balance of profits and gains for the year. The Indian Income-tax Act contains an express allowance or enumeration of deductions. In determining whether a particular item may or may not be deducted from the profits, it is necessary to inquire whether the deduction is expressly allowed.

The item of costs incurred by an assessee in litigation arising out of a business has not been specifically mentioned as one of the allowances permissible under the Indian Income-tax Act nor has it been prohibited under the English Income Tax Act. In *Commissioner of Income-tax, Bihar & Orissa* v. *Kameshwar Singh*[1], the Privy Council affirmed the decision of the Patna High Court in *Income-tax Commissioner, Bihar & Orissa* v. *Kameshwar Singh*[2]. The question was whether an expenditure of Rs. 2,07,018 incurred by an assessee in defending a suit which had been filed against his father for damages for the breach of contract arising out of the money-lending transaction was a deductible item. The decision was that the defence to the action was just as essential for the full protection of his rights as the creditor in the loan of rupees ten lakhs, as was his suit for the recovery of the loan, and that the item of expenditure in defence was an admissible item of expenditure under Section 10 (2) (ix) of the Income-tax Act.

A reference has been made in the order of the Appellate Tribunal to the decision in *Commissioner of Income-tax, Burma* v. *Gasper and Co., Rangoon*[3]. This was a case which was governed by the Income-tax Act before the amendment. A firm of partners had been importing for a number of years certain brands of whisky and brandy from a company in Calcutta. The individual partners of the firm and the manager of the liquor department were prosecuted for an offence against the Excise Act in Calcutta on criminal charges of conspiracy. The question was whether the expenditure was a permissible item of deduction under Section 10 (2) (ix) of the Income-tax Act for determining the profits of the firm for assessment. It was decided that it was not so permissible. The reason given for disallowing the expenditure was that the assessees incurred the expenditure to save the individual partners from the possible adverse consequences of a criminal conviction and not solely for the purpose of earning profits or gains in a business carried on by them. The judgment stressed the words "for the purpose of earning such profits" in clause (ix) of the section before its amendment and

(1) (1942) 10 I.T.R. 214; 23 Pat. 491.
(2) (1940) 8 I.T.R. 52.
(3) (1940) 8 I.T.R. 100.

stated that in the circumstances of the case it could not be said that at the time the criminal charge was brought against them the purpose which they intended to effect was to do more than secure acquittals in respect of each charge. The clause has now been amended, the limitation "for the purpose of earning such profits" has been removed and under the law as amended the expenditure should be "for the purpose of such business." The two expressions are not synonymous. The case cannot be treated as an authority for the interpretation of the amended clause (xii) which is in different terms from the original clause (ix) before its amendment by the Income-tax (Amendment) Act, VII of 1939. The case is of doubtful authority even in respect of clause (ix) of the section before its amendment especially after the decision of the Privy Council cited above.

The learned counsel for the Commissioner of Income-tax relied on the decision in *In the matter of Amrita Bazar Patrika Ltd.*[1], The assessee, the Amrita Bazar Patrika Ltd., carries on the business of editing, publishing and selling the paper called "The Amrita Bazar Patrika." A leader was published in that paper under the caption "Calcutta High Court" which contained certain observations which reflected upon the independence of the judiciary. The editor and printer of the newspaper were found guilty of contempt of Court by the Calcutta High Court, the former sentenced to three months' simple imprisonment and the latter to one month's imprisonment. The judgment is reported in *In the matter of Tushar Kanti Ghosh*[2]. The company incurred an expense of Rs. 5,577-7-9 in defending the editor and the printer and claimed that this item should be deducted in determining the profits of the business of the company. This was disallowed. The case was governed by Section 10 before its amendment by Act VII of 1939. The item was disallowed on two grounds, *viz.*, (i) the payment of this sum in no way assisted the company in earning profits or gains in the year of assessment and (ii) the business could be carried on without any infraction of the law. In the case under reference before us the expenditure was incurred for the purpose of the business and it has not been established that the assessee committed any breach of the law. The decision in *In the matter of Amrita Bazar Patrika Ltd.*[1] is, therefore, not applicable to the present case.

In *Strong & Co., Ltd.* v. *Woodifield*[3], the decision was that the item of £1,490 incurred on account of damages and costs was not a deductible item of business loss in computing the profits of the

(1) (1937) 5 I.T.R. 648.
(2) (1935) 63 Cal. 217.
(3) [1906] A.C. 448.

company for income-tax purposes. A brewery company owned an inn which was carried on by a manager as a part of their business. A customer sleeping in the inn was injured by the fall of a chimney and recovered damages and costs against the company for the injury which was owing to the negligence of the servants of the company. Lord Loreburn, L.C., held that only such losses can be deducted as are connected with it in the sense that they are really incidental to the trade itself and they cannot be deducted if they are merely incidental to some other vocation or fall on the trader in some character other than that of the trader and observed :—

"No degree of ingenuity can frame a formula so precise and comprehensive as to solve at sight all the cases that may arise. In the present case, I think that the loss sustained by the appellants was not really incidental to their trade as inn-keepers, and fell upon them in their character not of traders but of house-holders."

In *Commissioners of Inland Revenue* v. *E. C. Warnes & Co., Ltd.*[1], the respondent company carried on the business as oil merchants and was sued for a penalty on an information by the Attorney-General under Section 5 (1) of the Customs (War Powers) Act, 1915, for breach of certain orders and proclamations relating to the requirements of the Board of Customs and Excise with respect to a consignment of oil shipped by the company to Norway. The action was settled by consent on the agreement of the company to pay a mitigated penalty of £ 2,000, such sum to cover the costs of the Crown. In defending the proceedings the company incurred legal costs amounting to £ 560 18s. 10d. Rowlatt, J., held that the liability created by the section was of a penal character and observed :—

"I think that a loss connected with or arising out of a trade must, at any rate, amount to something in the nature of a loss which is contemplable, and in the nature of a commercial loss. I do not intend that to be an exhaustive definition, but I do not think it is possible to say that when a fine, which is what it comes to, has been inflicted upon a trading body, it can be said that that is 'a loss connected with or arising out of' the trade within the meaning of this Rule."

The decision was that the mitigated penalty and costs were not a loss connected with and arising out of the company's trade within the meaning of Rule 3, Case I, Schedule D, of the Income Tax Act, 1842, and that they were, therefore, not deductible in arriving at the profits of the company's trade for excess profits duty purposes. The same principle was involved in *Commissioners of Inland Revenue* v. *Alexander Von*

(1) (1919) 12 Tax Cas. 227.

Glehn & Co., Ltd.[1] The respondent company carried on business as general produce merchants and exported goods to Russia and Scandinavia and was sued for penalties under the Customs (War Powers) Act, 1915, on informations by the Attorney-General, in respect of infringements of that Act, in the course of its trade. The actions were settled by consent on the company agreeing to pay a compromise penalty of £3,000. The company incurred legal costs amounting to £1,074 12s. 7d. in respect of the proceedings. The Court of Appeal affirmed the order of Rowlatt, J., in the case and held that the mitigated penalty and costs were not admissible deductions in arriving at the profits of the company's trade for excess profits duty purposes. Lord Sterndale, M.R., at page 235 observed :—

" They certainly are proceedings in which a penalty is being sued for by the Attorney-General as representing the Crown, for an infraction of the law, whether technically criminal for the purpose of appeal seems to me to be immaterial. The money which is paid is money paid as a penalty......"

Further at page 238 : " . . . they committed a breach of the law, and for that breach of the law they were fined, and that does not seem to me to be a loss connected with the business, but it is a fine imposed upon the company personally, . . . for a breach of the law which they had committed. It is perhaps a little difficult to put the distinction into very exact language, but there seems to me to be a difference between a commercial loss in trading and a penalty imposed upon a person or a company for a breach of the law which they have committed in that trading. "

Scrutton, L. J., stated at page 244 : " Were these fines made or paid for the purpose of earning the profits ? The answer seems to me obvious, that they were not, . . . I do not wish to decide until I have heard the matter further argued, whether compensation paid in civil proceedings for carrying on business in a negligent way can or cannot be deducted from the profits."

The assessee Seth Chhaganmal Mangilal was not convicted for infringement of the trade mark. The suit against him was not decided on merits. An appeal was filed against an interlocutory order in a pending suit. The compromise of the claim did not amount to an admission that he had committed an infringement of the trade mark. Instead of carrying on an expensive and uncertain litigation he considered it more prudent to compromise the claim in order to minimise his losses or to save him from the payment of damages in case the suit

(1) (1920) 12 Tax Cas. 232.

was ultimately decided against him. The amount of Rs. 2,000 which he paid was not on account of a penalty for infringement of the trade mark but was solely on account of costs incurred by the plaintiff in the suit. The assessee in his memorandum of appeal before the Income-tax Appellate Tribunal was merely describing the nature of the suit which was filed against him and the statement did not amount to an admission that he had committed an infringement of the trade mark. In the carrying on of his business he was involved in a litigation and he was bound to defend the case and conduct it in a prudent manner which would be for his benefit and would minimise his losses. The expenditure was laid out or expended wholly and exclusively for the purpose of such business. The principle enunciated in the English cases referred to above is not applicable to the present case. In *Commissioner of Income-tax, C. P. and U. P.* v. *Mathuradas Mannalal* [1], a Divisional Bench of this Court held that the expenditure incurred by the assessee in avoiding a business liability was an allowable expenditure under Section 10 (2) (ix) of the Income-tax Act in the year in which the expenditure was actually incurred. The assessee in that case entered into certain forward contracts for the purchase and sale of cotton and these contracts resulted in losses which the assessee was not able to meet and a suit was instituted against him. The litigation extended for some years and was eventually compromised. A sum of Rs. 2,382 was incurred in defending the suit and he claimed this as a business expense and it was allowed.

In *Scammell & Nephew Ltd.* v. *Rowles* [2], the claim was by the appellant to deduct for the purpose of ascertaining their taxable profits three items, (i) £ 7,500 paid by the company to one of their directors, Mr. Hood Barrs, (ii) £ 62 10 s. being a contribution paid by them to a Mr. Toms towards his costs of certain litigation and (iii) £ 53 10s. representing costs incurred by them in connection with a compromise agreement. The claim was allowed by Lawrence, J., as deductible items of expenditure. The Court of Appeal affirmed his decision. Sir Wilfrid Greene, M.R., observed at page 349 :—

". . . that the compromise was a compromise effected for the purpose of the company's trade, and for the purpose of enabling them to recover the payment of a trading debt owing to them from a customer, which would come into computation in their trading account. On that basis, payments made as a condition of obtaining that compromise which secured that payment to them would have been payments wholly and exclusively laid out or expended for the purposes of the appellant company's trade."

(1) (1942) 10 I.T.R. 95. (2) (1939) 1 All E.R. 337 ; 8 I.T.R. Suppl. 41, at p. 53.

At page 351 he further observes :—

"In the present case, if the trading relation was one that was disadvantageous to the company and, in order to get rid of it, the company had to enter into an agreement with Mr. Toms and Blue Belle Motors, and, if, in order to secure that that agreement should be effective, it was necessary to make a payment to a third party, to wit, Mr. Hood Barrs, who was in a position to block the agreement, because his consent was necessary, and there was no means of compelling him to give it, the payment made to Mr. Hood Barrs was, it seems to me, a payment that was made for, and was directly connected with, the procuring by the company of the advantage of terminating that trading relation, and, as such, was wholly and exclusively laid out for the purposes of the company's trade."

£ 7500 which was paid by the company to Mr. Hood Barrs for compromising his action for damages for libel was allowed as a deductible item of expenditure; similarly the other two items were also allowed. The expression "capital expenditure" has not been defined either in the English or the Indian Income-tax Act. No precise, full and accurate definition of the phrase is to be found in the cases. Various tests have been formulated in several cases in determining whether an expenditure is a capital expenditure or a revenue expenditure. In *Vallambrosa Rubber Co., Ltd.* v. *Farmer*[1], at page 536, Lord Dunedin as President, stated :—

". . . in a rough way I think it is not a bad criterion of what is capital expenditure as against what is income expenditure to say that capital expenditure is a thing that is going to be spent once and for all, and income expenditure is a thing that is going to recur every year."

This rule has been amplified by Lord Cave in *British Insulated and Helsby Cables* v. *Atherton*[2], at page 213. After quoting the passage above cited Lord Cave observed :—

"But the criterion suggested is not, and was obviously not intended by Lord Dunedin to be, a decisive one in every case; for it is easy to imagine many cases in which a payment, though made 'once and for all' would be properly chargeable against the receipts for the year." and instances were given in which though the expenditure was incurred once and for all yet it was treated as a revenue expenditure and a permissible deduction. Lord Cave summed up in these terms :—

"But when an expenditure is made, not only once and for all, but with a view to bringing into existence an asset or an advantage for the enduring benefit of a trade, I think that there is very good reason

(1) (1910) 5 Tax Cas. 529. (2) [1926] A.C. 205; 10 Tax Cas. 155, at p. 192.

(in the absence of special circumstances leading to an opposite conclusion) for treating such an expenditure as properly attributable not to revenue but to capital."

Applying the test formulated by Lord Cave to the present case there can be no doubt that the expenditure did not bring into existence an asset or an advantage for the enduring benefit of a business. The expenditure of Rs. 3,351 was an expenditure which was properly attributable to revenue and not to capital. A payment made to a director whose services are dispensed with has been allowed as a deductible item of expenditure in *Mitchell* v. *B.W. Noble Ltd.*[1] A payment made for cancelling a contract of agency which became onerous was allowed as a deductible item of expenditure in *Anglo-Persian Oil Co.* v. *Dale*[2]. The legal expenses of defending the title to business premises abroad were allowed in *Southern* v. *Borax Consolidated Ltd.*[3] In *Kangra Valley Slate Co. Ltd.* v. *Commissioner of Income-tax, Punjab*[4], it was held that the expenditure incurred by the assessee-company in defending, as lessees of certain land, a suit for ejectment and injunction instituted by the lessors was a capital expenditure and was not a deductible item of expenditure under Section 10 (2) (ix) of the Income-tax Act. This decision is in conflict with the decision in *Southern* v. *Borax Consolidated Ltd.*[3], and has been disapproved in a Nagpur case. The case law on the subject has recently been reviewed in *Income-tax Appellate Tribunal, New Delhi* v. *Empress Mills, Nagpur*[5]. We respectfully agree with that decision. In that case it was held that legal expenses incurred by a company in protecting its trade mark is not in the nature of capital expenditure but is a revenue expenditure and as such is a proper deductible item in computing the taxable income of the company. This was a case where the assessee filed a suit in order to protect his trade mark from infringement. The principle enunicated in this decision is applicable to a case where the assessee is a defendant and defends the suit in order to protect the use of his trade mark. Our answer to the first question is, yes. As our answer to the first question is in the affirmative the second question does not fall for decision. The amount of Rs. 200 deposited by the assessee for reference to the High Court be refunded to him. The Commissioner of Income-tax will bear the costs of this reference. Counsel's fee Rs. 50.

Reference answered accordingly.

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(1) (1926) 11 Tax Cas. 372.
(2) (1931) 16 Tax Cas. 253.
(3) [1941] 1 K.B. 111; 10 I.T.R. Suppl. 1.
(4) (1935) 3 I.T.R. 324.
(5) (1943) 11 I.T.R. 266.

[IN THE CALCUTTA HIGH COURT.]

COMMISSIONER OF INCOME-TAX, BENGAL

v.

GOSTHA BEHARI SADHUKHAN AND OTHERS*.

GENTLE and ORMOND, JJ. January 17, 1946.

INDIAN INCOME-TAX ACT (XI OF 1922), SECS. 25, 26-A—HINDU UNDIVIDED FAMILY—FAMILY BUSINESS—FORMATION OF PARTNERSHIP WITH STRANGERS WITHOUT PARTITION—LEGALITY—APPLICATION FOR REGISTRATION OF FIRM.

A Hindu undivided family consisting of A and his three nephews B, C and D, owned a business and the family was being assessed as such until 1941-42. On the 15th June, 1942, a deed of partnership was made between A of the first part, B representing himself and his two brothers C and D of the second part, and three other persons who had been for many years employees of the business. The deed recited that the parties had been carrying on the business jointly till 13th April, 1939, and had agreed to carry it on as partners and the respective shares of the partners were also specified in the deed. An application for registration of the firm under Section 26-A of the Indian Income-tax Act was rejected by the Income-tax Officer on the ground that there was no evidence of partition and the firm could not therefore be recognised :

Held, *that it was a preliminary to the registration of the partnership firm sought to be registered that there should have been a partition of the Hindu undivided family previously owning the business and that in the absence of proof of such partition the Income-tax Officer was right in refusing registration.*

Cases referred to :—

Jattu Shah Nathu Shah *v.* Commissioner of Income-tax, Punjab and N.W.F. Provinces [1932] (138 I.C. 187 ; A.I.R. 1932 Lah. 575; 14 Lah. 134 ; 6 I.T.C. 162).

S. C. Mullick & Sons, *In re* [1938] (6 I.T.R. 99).

P. K. P. S. Pichappa Chettiar *v.* Chokalingam Pillai [1934] (38 C.W.N. 1185).

Reference by the Income-tax Appellate Tribunal under Section 66 (1) of the Indian Income-tax Act, 1922 : Reference No. 8 of 1944.

STATEMENT OF CASE.

"This is an application under Section 66 (1) of the Income-tax Act by the Commissioner of Income-tax, Bengal, requiring the following

* [It is to be regretted that the decision of the Privy Council in *Sir Sundar Singh Majithia's case* [1942] (10 I.T.R. 457) was not brought to the notice of the learned Judges.—*Ed.*]

question to be referred to the High Court at Calcutta. It is stated that the question arises out of the order of the Appellate Tribunal in 26 A. R. A. No. 4 of 1943-44 in the case of Gostha Behari Sadhukhan and others. The question required to be referred is:

'Whether, in the facts and circumstances of the case, the Tribunal were right in law in holding that there was no legal impediment to the recognition of a partnership as respects the Gopal Pure Oil Mills between the applicants under Section 26-A of the Indian Income-tax Act.'

In the reply submitted by the respondent under rule 54 of the Appellate Tribunal Rules, it is submitted the question framed is not one of law, that the only point that may arise is whether a Hindu undivided family can enter into partnership with strangers in regard to a business carried on by the family hitherto and the answer to this question is "so simple and well accepted that no reference is needed."

In the order of the Appellate Tribunal in the case under consideration it has been held that there is no impediment legal or otherwise to recognise this contractual relationship between the five persons as one of partnership. The question raised by the applicant is obviously one of law and we accordingly proceed to state the case :—

A Hindu undivided family was carrying on the business of pressing and sale of oil under the style of Gopal Pure Oil Mills. Gostha Behari Sadhukhan and Sarat Chandra Sadhukhan were two members of this Hindu undivided family. A partnership was formed for carrying on the said business between five persons, Gostha Behari Sadhukhan, Amulya Charan Samanta, Jugal Krishna Das, Kartick Chandra Pramanick and Sarat Chandra Sadhukhan as representative of the Hindu undivided family of which he was a member. The relative deed dated 15th June, 1942, was filed for purposes of registration with the Income-tax Officer under Section 26-A of the Income-tax Act.

The Income-tax Officer refused to recognise the respondent as a firm as according to him Gostha Behari Sadhukhan and Sarat Chandra Sadhukhan had no power to form a partnership as distinct from the Hindu undivided family of which they were members as the joint family properties had not been partitioned. In appeal the Appellate Assistant Commissioner held that the business of oil milling was owned by the Hindu undivided family and the formation of a partnership as aforesaid in respect of this business was not legally possible.

In disposing of the appeal, the Appellate Tribunal held that the partners of the firm formed by the partnership were five, (1) the undivided Hindu family as such, which was hitherto the owner of the business, represented by Sarat Chandra Sadhukhan, (2), (3) and (4) the

three other strangers to this family, Amulya Charan Samanta, Jugal Krishna Das and Kartick Chandra Pramanick, and (5) Gostha Behari Sadhukhan, a member of the said family for himself. The Appellate Tribunal also held that a Hindu undivided family can enter into a partnership with strangers in respect of any business carried on by the family before such formation and there was no legal impediment to recognise the contractual relationship between the said five persons in respect of the business that was carried on by them together.

It may be pointed out at this stage that the statements made by the applicant in paragraph 4 of the application are not correct. In 4 (1) the applicant states that the Appellate Tribunal had misdirected themselves about the importance of the fact that a partition had not been proved. It may be observed as aforesaid that the Tribunal held that in respect of a business owned by a Hindu undivided family (*sic*) between the Hindu undivided family as such and strangers and as such the question of any partition of the properties of the family does not arise in respect of a partnership of which the family as a unit is a partner with strangers.

In paragraph 4 (2) the applicant states that the Appellate Tribunal has held that there were two families that were partners in this partnership of five persons. As a matter of fact it will be found that the Appellate Tribunal held that there was only one family represented by Sarat Chandra Sadhukhan, a partner in this partnership.

On the findings of the Appellate Tribunal as aforesaid the question of law raised by the applicant does arise. As regards the form it may be stated more directly, either, 'whether the relationship between the five persons as evidenced by the deed dated 15th June, 1942, is one of partnership under the Partnership Act, 1932," or, 'is there any legal impediments to the recognition of the partnership.'

The above question is therefore referred to the High Court under Section 66 (1) of the Income-tax Act."

S. K. Gupta with *J. C. Pal*, for the Commissioner.

Gopendra Nath Das with *Sambhu Nath Banerjee* and *Manindra Nath Ghosh*, for the assessee.

JUDGMENT.

GENTLE, J.—This is a reference by the Income-tax Appellate Tribunal at the instance of the Commissioner of Income-tax, Calcutta. The facts concerned can shortly be stated as follows :—For many years a business known as Gopal Pure Oil Mills was owned by a Hindu

undivided family the members of which were Gostha Behari Sadhukhan and his three nephews, Sarat Chandra Sadhukhan, Rabindra Nath Sadhukhan and Panchkari Sadhukhan. Up to and including the year of assessment 1941-42, this business was assessed as a Hindu undivided family. On the 29th October, 1942, an application was made to the Income-tax Officer under Section 26-A (1) of the Income-tax Act to register a deed of partnership. The Income-tax Officer refused to register it. The deed of partnership is dated 15th June, 1942, made between Gostha Behari of the first part, Sarat purporting and stating as representative of himself and his brothers Rabindra and Panchkari of the second part, and three other persons, Amulya Charan Samanta, Jugal Krishna Das and Kartick Chandra Pramanick, who were, and had been for many years employees of the business. The deed recites that the parties, which clearly means Gostha Behari and Sarat, had been carrying on the business jointly till the end of the year 1345 B. S. corresponding to the 13th April, 1939, and for better management of the business the parties agreed to carry on the business as partners. The shares in the partnership are divided as to Gostha 5 as. 6 ps., Sarat 5 as. 6 ps., Amulya 2 as. 9 ps., Jugal 1 a. 3 ps., and Kartick 1 anna. The Income-tax Officer was not satisfied that previous to the execution of the partnership deed the business had been the subject of partition amongst the members of the family above mentioned and he refused to register the deed of partition and assessed the profits of the business on the basis of a Hindu undivided family.

An appeal by the assessee was dismissed by the Appellate Assistant Commissioner on the 23rd June, 1943, but a further appeal was allowed by the Appellate Income-tax Tribunal by their order dated the 11th December, 1943. The Commissioner of Income-tax being dissatisfied with this order obtained a reference under Section 66 of the Act from the Appellate Tribunal for the following question to be answered by this Court:—

"Whether the relationship between the five persons as evidenced by the deed dated 15th June, 1942, is one of partnership under the Partnership Act, 1932," or, in the alternative, "Is there any legal impediments to the recognition of the partnership."

It is common ground that, before the deed of partnership could have been made between Gostha and Sarat and the other three parties in respect of the business, that property of the joint Hindu family would require previously to have been partitioned.

Section 25-A (1) of the Act provides:—

"Where, at the time of making an assessment under Section 23, it is claimed by or on behalf of any member of a Hindu

family hitherto assessed as undivided that a partition has taken place among the members of such family, the Income-tax Officer shall make such inquiry thereinto as he may think fit, and, if he is satisfied that the joint family property has been partitioned among the various members or groups of members in definite portions he shall record an order to that effect :

Provided that no such order shall be recorded until notices of the inquiry have been served on all the members of the family."

Sub-section (3) *ibid* provides:—

"Where such an order has not been passed in respect of a Hindu family hitherto assessed as undivided, such family shall be deemed, for the purposes of this Act, to continue to be a Hindu undivided family."

Learned Counsel on behalf of the assessee contended that the partnership deed shows there had been a partition of the business and it must and should have been taken by the Income-tax Officer, as he says, at its face value, and that the statements in it should have been accepted unless the Income-tax Officer could have found anything on materials or evidence to disprove what it says. To support the contention that the document shows that there was a partition with respect to the business, learned Counsel pointed out that Sarat was executing the document as representative of himself and his three brothers. This, it was contended, should establish, at any rate, sufficiently for the Income-tax Officer, that the business had been separated from the other assets of the family. Further in the document, learned Counsel argued, there is a recital that the parties had been carrying on business jointly till the end of the year 1345 B.S.; from that it should have been accepted by the Income-tax Officer that on the 13th April, 1939, which corresponds to the date I have just mentioned in the Bengali calendar, there was a partition. He argued that the later statement was evidence, which should have been accepted, of such disruption. If that were correct then nothing would be easier for anyone than to place a piece of paper before the Income-tax Officer who should be bound to accept what is stated in that paper and be obliged to act upon it. That is not as I read Section 25-A of the Act. That section requires that when a member of a Hindu family, hitherto assessed as undivided, alleges that a partition has taken place the Income-tax Officer shall make an order recording the contention if he is satisfied that there has been a partition. That does not mean that he must accept the *ipse dixit* of the person whose paper, I have mentioned, is placed before him. The proviso to Section 25-A (1) is to the effect that no such order shall be recorded until notices of the inquiry have been served on all the members of the family. Clearly the

section contemplates that when a claim of the nature with which we are now dealing has been made all those persons previously interested should be given an opportunity of attending before the Income-tax Officer to dispute it, if such be the case. In the case of *S. C. Mullick & Sons* [1], it was held that though the recitals in a partnership deed may be evidence and even conclusive evidence as between the parties to it, the Income-tax department is not bound to accept them as correct and can call upon the executants thereof to prove the facts recited therein. In the present case there was no evidence of partition apart from the recital and statement in the deed of partnership, even assuming that that recital and statement bear the meaning for which learned Counsel for the assessee has contended. Nothing would have been easier than to have had some evidence of a previous partition, prior to the partnership deed having been executed.

In the case of *Jattu Shah Nathu Shah* v. *Commissioner of Income-tax, Punjab and N. W. F. Provinces*[2], two deeds were placed before the Income-tax Officer, in one of which there was a statement that the joint family had already been disrupted, and in the other that the family had been divided since a long time. That was a case in which a decision under the provisions of Section 25-A of the Act was given and it was held that those bare statements in the two deeds were insufficient to establish a separation or partition of the property.

In my opinion, there was nothing before the Income-tax Officer which would justify him coming to the conclusion that the business known as Gopal Pure Oil Mills had ceased to belong to a joint Hindu family, the members of which were an uncle and his three nephews. Until there had been a partition none of the members of the family could enter into a partnership with three strangers in respect of that business.

It is to be further observed that the Income-tax Tribunal having arrived at a different conclusion to that to which the Appellate Assistant Commissioner and the Income-tax Officer had come, I can see no reference in their order that notices should be given under the proviso to Section 25-A (1) of the Act to enable the other members of the joint family to appear and object to an order being made.

In my view, the Income-tax Officer arrived at the correct decision and conclusion and that the reversal of his finding and also that of the Appellate Assistant Commissioner by the Income-tax Tribunal was wrong. The questions which are referred are not too happily phrased but I answer the second alternative question "Is there any legal impediments to the recognition of the partnership" in the affirmative.

(1) (1938) 6 I.T.R. 99. (2) (1932) 6 I.T.C. 162; 14 Lah. 134.

ORMOND, J.—It is established that the Income-tax Officer need not accept the deed of partnership offered to him for registration under Section 26-A of the Income-tax Act or its recital as correct. For authority as to this it is sufficient to refer to the case of *Jattu Shah Nathu Shah* v. *Commissioner of Income-tax, Punjab & N. W. F. Provinces*[1]. In that case in fact the Income-tax Officer on enquiry came to a finding against the declaration in the deed. The terms of the deed of partnership were set out from page 165 onwards and the declarations that the family had been disrupted and that they were carrying on the business as two firms are to be seen from the translations of the partnership deeds there set out. It is for us in this Court to proceed on the facts found and put before us on the record and the statement of the case. In this particular case it is evident from the findings of fact, from the Income-tax Officer onwards, that there was, in fact, no partition of the Hindu undivided family business which previously to the application to register the partnership firm had been the owners of the same business. Section 5 of the Partnership Act categorically provides that members of a Hindu undivided family are not partners. As soon therefore as it was shown to the Income-tax authorities that it was one and the same business in respect of which an application is now being made to register as owners of the partnership firm which had previously been the property of the Hindu undivided family, it is clearly in the interest of justice that the Income-tax Officer should make an enquiry to ascertain not only that the persons seeking to be registered as new owners were agreeable to this course, but that the members of the Hindu undivided family who previously owned the business were also agreeable. This is provided for in Section 25-A making it necessary, as my learned brother has pointed out, that notices are first to be served on all the members of the family; and that "where any claim is made on behalf of any member of a Hindu family, hitherto assessed as undivided, that a partition has taken place" the Income-tax Officer is to make an enquiry and is to be satisfied that the joint family property has been partitioned; and that only then is he to record an order to that effect. In the present case the nature and the circumstances, in which the application for the registration of the partnership firm was made, appear from page 4 of the paper book in the judgment of the Income-tax Officer where he says:—

"Referring to the partnership deed, dated 15th June, 1942, he (the pleader) states that Babus Gostha Behari Sadhukhan and Sarat Chandra Sadhukhan, members of a Hindu undivided family and still

(1) (1932) 6 I.T.C. 162; 14 Lah. 134.

continuing as such, separated from the assets of the Hindu undivided family the business styled Gopal Pure Oil Mills and formed themselves into a firm by taking in three of their former employees as working partners . . ."

This recital and the circumstances in which the application was made clearly leave no doubt in my mind that Section 25-A was attracted; and the procedure under Section 25-A was made a requisite preliminary step in this case before the partnership firm could be registered.

For authority that the partnership sought to be registered is to be limited to the signing parties, reference may be made to the case of *P. K. P. S. Pichappa Chettiar* v. *Chokalingam Pillai*[1]. Since Rabindra and Panchkari did not sign the application it follows that they could not be regarded as members of the new partnership firm sought to be registered. Rule 2 of the Indian Income-tax Rules, moreover, expressly stipulates that the application for registration under Section 26-A of the firm is to be signed by all the partners personally. It follows from this that Rabindra and Panchkari though they had been members of the Hindu undivided family and were accordingly two of the joint owners of the Hindu family business, were not by virtue of the application for registration to be partners in the firm sought to be registered. Even if it could be contended for the assessee that for other members of the Hindu undivided family the mere filing and signing of the application for registration as a firm under Section 26-A in itself amounted to proof both of partition and of their consent to partition and by reason of their presence before the Income-tax Officer afforded an excuse for non-issue of notice under Section 25-A, yet no such contention would be open to the assessee in regard to Rabindra and Panchkari.

In these circumstances and for these reasons, as well as those stated by my learned brother in his judgment, I agree that it was a preliminary to the registration of the partnership firm sought to be registered that there should have been a partition of the Hindu undivided family previously owning the business; and that in the absence of proof of such partition, the Income-tax Officer was right in refusing registration and I concur in the answer to the question given by my learned brother.

Reference answered accordingly.

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(1) (1934) 38 C.W.N. 1185.

[IN THE MADRAS HIGH COURT.]

COMMISSIONER OF INCOME-TAX, MADRAS

v.

SRI TALUPURU VENKATASUBBIAH CHETTY.

SIR LIONEL LEACH, C.J., and PATANJALI SASTRI, J.

November 23, 1945.

INDIAN INCOME-TAX ACT (XI OF 1922), SEC. 10 (2) (xi)—BAD DEBT—MONEY-LENDING BUSINESS—DISSOLUTION OF FIRM—DEBTS ALLOTTED TO JOINT HINDU FAMILY ON DISSOLUTION ENTERED IN ITS BOOKS—INTEREST PAID ASSESSED TO INCOME-TAX—SUBSEQUENT WRITING OFF OF DEBTS AS BAD AND IRRECOVERABLE—WHETHER AMOUNT ALLOWABLE DEDUCTION.

The assessee was the manager of a Hindu undivided family which carried on a money-lending business. In 1933 a separate money-lending business carried on in partnership by the family with another person was dissolved and the family received as part of its share certain promissory notes executed by persons to whom the partnership had lent money. These debts were entered in the books of the family relating to its own money-lending business and the promissory notes were renewed from time to time. The interest paid to the family by the debtors was included in the profits of the family and assessed to income-tax accordingly. In the year of account, 1941-42, the assessee wrote off as being irrecoverable three debts and claimed to deduct the amount from the assessable income under Section 10 (2) (xi) of the Indian Income-tax Act:

Held, *that the amount was allowable as a deduction in the assessment for 1942-43 under Section 10 (2) (xi) of the Indian Income-tax Act.*

Case referred to:

Chimanram Rameswarlal *v.* Commissioner of Income-tax, Bengal [1940] (8 I.T.R. 408).

Case referred to the High Court by the Income-tax Appellate Tribunal, Madras Bench, under Section 66 (1) of the Indian Income-tax Act, 1922 (Act XI of 1922), as amended by Section 92 of the Income-tax (Amendment) Act, 1939 (Act VII of 1939), in Application No. 66 R. A. No. 16 (Madras) of 1944-45 on its file (assessment year 1942-43) for decision on the following question of law :—

"Whether on the facts and in the circumstances of the case, the sum of Rs. 8,855 is allowable as a deduction in the assessment for 1942-43 under Section 10 (2) (xi) or any other provisions of the Income-tax Act?"

Case Referred No. 6 of 1945.

STATEMENT OF CASE.

" This is an application under Section 66 (1) of the Income-tax Act made by the Commissioner of Income-tax, Madras, against an order dated 11th May 1944 passed by the Tribunal in R.A.A. No. 2 (Madras) of 1943-44. The question framed by the Commissioner is as follows :—

'Whether on the facts and in the circumstances of the case, the sum of Rs. 8,855 is allowable as a deduction in the assessment for 1942-43 under Section 10 (2) (xi) or any other provisions of the Income-tax Act ?'

2. The facts of the case are as follows :—

There was a partnership firm known as Talupuru Subbaramaniam Chetty and Co., (corrected by the Commissioner of Income-tax in his application as "Talupur Subramaniam Chetty & Sons "). According to the facts stated by the Income-tax Officer at page 3, lines 6 to 8, it appears that the firm's name was Talupur Subbaramayya Chetty & Co. The same name has been quoted by the Appellate Assistant Commissioner in his appellate order, page 2 [contention (iii)], lines 3 and 4. In this (defunct) concern the father of the respondent was a partner along with one Chinni Veeraswami Chetti. In the year 1933 the partnership was dissolved and in 1934 the assets of the firm were divided and the respondent's family got, by way of its share, some debts covered by promissory notes. We understand that the family had money-lending business apart from business in timber, iron and hardware.

3. In his books of account dealing with the money-lending business he had entered these debts as part of his money-lending assets. In 1936-37 assessment, the Department treated these debts as part of the money-lending capital and taxed interest realised on these debts. In an appeal against 1936-37 assessment one such debt was allowed as bad debt. Whenever interest accrued to the respondent on these promissory notes, according to the system of accounting of the assessee the Department taxed the respondent on this accrued interest. In the present year of assessment, *i.e.*, 1942-43, a sum of Rs. 2,866, interest on one of these debts, had been accounted for by the respondent as income from money-lending business and taxed by the Income-tax Officer, whereas a sum of Rs. 3,182 written off as bad debt relating to the same debt was disallowed as a loss. It may be stated here that the sum of Rs. 8,855 mentioned by the Commissioner consists of three different items of Rs. 3,182, Rs. 4,382 and Rs. 1,291.

4. In the assessment order for the year 1936-37 it has been specifically mentioned that the assets taken over from the discontinued firm by the respondent were treated by him as part of his money-lending capital. On these facts the Tribunal held that the debts were part of

his stock-in-trade inasmuch as they became the circulating capital and should be allowed as a trading loss or a bad debt.

5. The Departmental Representative urges that even if the Department has treated these debts as being incorporated in his money-lending business and assessed the income therefrom as interest, the allowance of bad debt is only governed by Section 10 (2) (xi) of the Act and, therefore, unless the respondent can bring it within the letter of that section no relief should be granted to him. The section recites, *inter alia*, that the debts must be the debts of money-lending business carried on by the respondent. He submitted that it cannot be urged that the debts in question were debts of the money-lending business carried on by the Hindu undivided family. The respondent, on the other hand, contends that the incorporation in the accounts of the money-lending business by the respondent in the present case would amount to a notional payment by the debtor and re-lending by the respondent. If the Department's contention is to be accepted, it would amount to this that no allowance for bad debt can ever be made to a money-lending creditor who has accepted transfer of a debt under circumstances outlined above or similar thereto, should that debt ever become bad.

6. In any case we think that a question of law does arise in this case and the question formulated by the Commissioner, as mentioned above, is referred to their Lordships for their opinion.

7. In this connection, we would like to add that in paragraph 4 (a) of the application by the Commissioner, it has been stated as follows :—

'That in arriving at the finding mentioned at item (3) of paragraph 3 of this application, the Bench appears to have committed an error which is apparent from the records, namely:

There is no reference to any income from money-lending business as such either in the assessment order in question or in the statement of profit and loss and the statement of income adjusted for income-tax purposes filed by the respondent.'

In paragraph 3, sub-clause (3), of the application, we have found :—

'That in the assessment for 1942-43 now in question, a sum of Rs. 2,866 representing interest on one of these debts was taxed as income from money-lending business.'

In the assessment order, middle of page 3, the Income-tax Officer has stated :—

'In the case of the debt of Nagareddi Venkatarama Reddi, the assessee obtained a fresh pronote from the debtor for a sum of Rs. 6,362 on 30th December 1941. The interest merged in the fresh

pronote, *viz.*, Rs. 2,866, was duly accounted for in the interest account.'

Besides, the Appellate Assistant Commissioner has stated in his order that the respondent carried on business in timber, iron, hardware and money-lending.

We cannot understand the reason why the learned Commissioner has made the above-referred statement in paragraph 4 (a) of his application."

C. S. Rama Rao Sahib, for the Commissioner.

P. R. Srinivasan, for the assessee.

JUDGMENT.

(Judgment of the Court was delivered by the Honourable the Chief Justice.)

The assessee is the manager of a joint Hindu trading family, which deals in timber, iron and hardware and runs a money-lending business. Before 1933 it carried on a separate money-lending business in partnership with one Chinni Veeraswami Chetti. This business was dissolved in 1933 and its assets were divided between the partners. As part of its share the family of the assessee received certain promissory notes executed by persons to whom the partnership had lent money. At the time of the dissolution these debts were regarded as being good and were entered in the books of the family relating to its own money-lending business. From time to time the promissory notes were renewed and interest was paid to the family by the debtors. This interest was included in the profits of the family and assessed to income-tax accordingly.

In the year of account, 1941-42, the assessee wrote off as being irrecoverable three debts, namely, Rs. 3,182, Rs. 4,382 and Rs. 1,291, making in all Rs. 8,855. The assessee claimed to be entitled to deduct this amount in calculating his assessable income by reason of the provisions of Section 10 (2) (xi) of the Indian Income-tax Act. The Income-tax authorities refused to recognize the validity of this course, but it was upheld by the Income-tax Appellate Tribunal, Madras Bench, in an order dated the 11th May 1944. At the instance of the Commissioner of Income-tax the Tribunal has referred to this Court under the provisions of Section 66 (1) the following question:—

"Whether on the facts and in the circumstances of the case, the sum of Rs. 8,855 is allowable as a deduction in the assessment for 1942-43 under Section 10 (2) (xi) or any other provisions of the Act."

Section 10 (2) (xi) allows a person carrying on a money-lending business to deduct loans made in the ordinary course of that business

when they are irrecoverable, provided that they do not exceed the amount actually written off as irrecoverable in the books of the assessee. In this case all the three debts were written off and it is accepted by the Commissioner of Incomè-tax that they are in fact irrecoverable. Mr. Rama Rao Sahib, on behalf of the Commissioner, says that the Tribunal erred in allowing the assessee's appeal because these loans were not made in the ordinary course of the family's business, but were made in the course of the partnership business. It is true that the money was actually lent by the partnership, but the loans were allotted to the family on the dissolution of the partnership and they became part of the assets of the family's own business. The promissory notes which were actually written off as irrecoverable were not the original promissory notes, but they were promissory notes which had been renewed by the borrowers in favour of the assessee. Inasmuch as the Income-tax authorities have since the dissolution regarded these loans as being part of the family's business and taxed the family on the interest paid in respect of them, it is rather surprising that they should now contend that clause (xi) does not apply. Since 1933 these loans have been regarded as having been made by the assessee in the ordinary course of its business. In fact, in the assessment for 1936-37 the assessee was allowed to deduct as irrecoverable another debt which it had received on the dissolution of the partnership.

Mr. Rama Rao Sahib, in the course of his argument, referred us to the decision of the Calcutta High Court in *Chimanlal Rameswarlal* v. *Commissioner of Income-tax, Bengal* [1], which he regarded as supporting his argument. The facts in that case do not appear to be on all fours with the facts in the present case and we do not regard it as being applicable. We reserve our opinion as to whether it should be followed by this Court until the question arises on exactly similar facts.

We answer the question referred by stating that the sum of Rs. 8,855 is allowable as a deduction in the assessment for 1942-43 under Section 10 (2) (xi).

The Commissioner will pay the assessee's costs, Rs. 250.

Reference answered accordingly.

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(1) (1940) 8 I.T.R. 408.

[IN THE MADRAS HIGH COURT.]

COMMISSIONER OF INCOME-TAX, MADRAS

v.

RAO BAHADUR RAVULA SUBBA RAO AND ANOTHER.

SIR LIONEL LEACH, C. J., and PATANJALI SASTRI, J.

February 22, 1946.

INDIAN INCOME-TAX ACT (XI OF 1922), SEC. 26-A—INCOME-TAX RULES, R. 6—POWERS-OF-ATTORNEY ACT, 1882, SEC. 2—FIRM—APPLICATION FOR RENEWAL OF REGISTRATION—SIGNATURE BY DULY AUTHORISED AGENT OF PARTNER—VALIDITY—"PERSONALLY" IN R. 6, MEANING OF.

The word "personally" in rule 6 of the Income-tax Rules as framed under Section 59 of the Indian Income-tax Act, 1922, would exclude a duly authorised agent of a partner from signing an application on behalf of the partner under Section 26-A of the Income-tax Act.

Section 2 of the Powers-of-Attorney Act, 1882, merely states the general principle of agency and it cannot override the specific provisions contained in rule 6 of the Income-tax Rules.

Case referred to the High Court by the Income-tax Appellate Tribunal under Section 66 (1) of the Income-tax Act, 1922 (Act XI of 1922), as amended by Section 92 of the Income-tax (Amendment) Act, 1939 (Act VII of 1939), in Application No. 26 (Madras) of 1944-45 on its file for decision on the question of law, namely, "whether the word 'personally' in rule 6 of the Income-tax Rules as framed under Section 59 of the Income-tax Act would exclude a duly authorised agent of a partner from signing an application on behalf of the partner under Section 26-A of the Income-tax Act?"

Case Referred No. 16 of 1945.

STATEMENT OF CASE.

"This is an application under Section 66 (1) of the Income-tax Act filed by the Commissioner of Income-tax, Madras, for reference of the following question of law to the Honourable High Court at Madras:—

'Whether in the circumstances of the case the application for renewal of registration was in accordance with the rules and whether the renewal was rightly refused to the respondent by the Income-tax Officer?'

The application arises from the Tribunal's order under Section 33, dated 6th June 1944, in 26-A Reg. A No. 13 (Madras) of 1943-44,

dismissing the appeal filed by the Income-tax Officer against the decision of the Appellate Assistant Commissioner.

2. The facts are that there is a firm consisting of two partners who are brothers, by name Ravula Subba Rao and Hariprasada Rao. Ravula Subba Rao had gone on a long pilgrimage. Before he went on pilgrimage he gave a general power-of-attorney to his brother, Hariprasada Rao, to manage his affairs. This power-of-attorney specifically gave his brother, Hariprasada Rao, power to 'represent me and sign and file all necessary papers, etc., in all Courts and offices.'

3. For the previous assessment year the partnership firm was registered under Section 26-A of the Indian Income-tax Act. For the assessment year under appeal the brother filed an application before the Income-tax Officer for renewal of such registration, which under the law, has to be made annually on a proper form. The applicant in this application signed for himself as well as for the brother, Ravula Subba Rao, whose power-of-attorney he held.

4. Under rule 6 of the rules framed by the Central Board of Revenue it is stated that an application for renewal of registration shall be signed 'personally' by all the members of the firm. The word 'personally' was inserted by Notification No. 78 of 1939. Before that, the rule was: 'such application shall be signed by all the partners of the firm.'

5. The Income-tax Officer, interpreting the rule strictly, held that the application was not properly presented inasmuch as the other partner on pilgrimage had not signed *personally*. The Appellate Assistant Commissioner, however, set aside the order of the Income-tax Officer on appeal and held that 'person' would include a legally authorised agent. Against that decision the Income-tax Officer appealed to the Tribunal on the ground that 'personally' would mean 'by the person himself' and not 'by an authorised agent.' We rejected the contention of the Income-tax Officer and dismissed his appeal holding with the Appellate Assistant Commissioner that 'personally' would include authorised agent and that the rule was altered with a view to stop unauthorised agents from signing on behalf of the partners. We also held that under the Powers-of-Attorney Act, VII of 1882, a statutory right has been given to a citizen by which a person is entitled by law to give authority to another person to do acts on his behalf so that the acts done will be deemed to be done by the person himself. Unless this right, which is vested in every person, is specifically abrogated or repealed by the Income-tax Act, the rules framed under the Income-tax Act cannot take away that right already vested in a person under that statute. The

rules are framed under Section 59 of the Income-tax Act for carrying out the purposes of the Act and for the ascertainment and determination of any class of income. The purpose of the Act is found in its preamble as being expedient to consolidate and amend the law relating to income-tax. We held that it cannot be the purpose of the Income-tax Act to give power to the framers of the rules to make such rules as would directly violate the right given to a citizen by another statute.

6. We think that a point of law does arise from our order and we, therefore, refer the following question of law for their Lordships' opinion :—

Whether the word 'personally' in rule 6 of the Income-tax Rules, as framed under Section 59 of the Income-tax Act, would exclude a duly authorised agent of a partner from signing an application on behalf of the partner under Section 26-A of the Income-tax Act?"

C. S. Rama Rao Sahib, for the Commissioner.

Advocate-General and *K. Krishnamurthi*, for the assessee.

JUDGMENT.

(Judgment of the Court was delivered by Patanjali Sastri, J.)

This reference arises out of an application made by one Hariprasada Rao before the Income-tax Officer for the renewal of the registration of a firm composed of himself and his brother Rao Bahadur Ravula Subba Rao. The application was rejected by the Income-tax Officer on the ground that it was not signed by both the partners personally as required by rule 6 of the rules made under Section 59 of the Indian Income-tax Act, 1922, which provides :—

"Any firm to whom a certificate of registration has been granted under rule 4 may apply to the Income-tax Officer to have the certificate of registration renewed for a subsequent year. Such application shall be signed personally by all the partners (not being minors) of the firm, or where the application is made after the dissolution of the firm by all persons (not being minors) who were partners in the firm immediately before dissolution and by the legal representatives of any such person who is deceased and accompanied by a certificate in the form set out below."

The assessee contended that as the other partner Ravula Subba Rao had gone on a long pilgrimage, he could not sign the application for renewal of the certificate of registration and that, as Hariprasda Rao held a general power of attorney from Ravula Subba Rao, his signature on behalf of the latter was sufficient compliance with the rule. The Income-tax Officer negatived this contention and rejected the application. On appeal to the Appellate Assistant Commissioner, the contention of the assessee was accepted with the result that the

order of the Income-tax Officer was set aside and he was directed to take the application on his file and dispose of it according to law. On appeal by the Officer to the Income-tax Appellate Tribunal, Madras Bench, the Tribunal concurred in the view of the Appellate Assistant Commissioner and dismissed the appeal. On application by the Commissioner of Income-tax under Section 66 (1) to state a case to this Court, the Appellate Tribunal has referred the following question for our decision :—

"Whether the word 'personally' in rule 6 of the Income-tax Rules, as framed under Section 59 of the Income-tax Act, would exclude a duly authorised agent of a partner from signing an application on behalf of the partner under Section 26-A of the Income-tax Act?"

It is contended for the Commissioner that the word "personally" used in the rule necessarily excludes acting by an authorised agent and that therefore the view taken by the Assistant Commissioner was erroneous in law. We agree with this contention. The learned Advocate-General appearing for the assessee has drawn attention to Section 2 of the Powers-of-Attorney Act, 1882, which reads thus :—

"The donee of a power-of-attorney may, if he thinks fit, execute or do any assurance, instrument or thing in and with his own name and signature, and his own seal, where sealing is required, by the authority of the donor of the power; and every assurance, instrument and thing so executed and done, shall be as effectual in law as if it had been executed or done by the donee of the power in the name, and with the signature and seal, of the donor thereof.

This section applies to powers-of-attorney created by instruments executed either before or after this Act comes into force."

The argument is that, by virtue of this provision, the act of Hariprasada Rao who, as has been stated, holds a general power-of-attorney from Ravula Subba Rao, in signing the application on behalf of the latter should be regarded as effectual in law as if Ravula Subba Rao had himself signed the application. We are unable to accept this view. The section merely states the general principle of agency and it cannot override the specific provisions of a rule made under a different statute which require that a particular act should be done by a person "personally," *i.e.*, by himself.

We answer the question referred accordingly in the affirmative.

The learned Advocate-General wished to raise the question that rules 2 and 6 are *ultra vires* the rule-making authority, the Central Board of Revenue. The question has not been referred to us and we express no opinion upon it.

The assessee will pay Rs. 250 for costs of the Commissioner.

Reference answered accordingly.

[IN THE MADRAS HIGH COURT.]

COMMISSIONER OF INCOME-TAX, MADRAS
v.
S. A. S. RAMASWAMY CHETTIAR.

SIR LIONEL LEACH, C. J., and PATANJALI SASTRI, J.

February 22, 1946.

INDIAN INCOME-TAX ACT (XI OF 1922), SEC. 10 (2) (xii)—LOSS—MONEY-LENDING BUSINESS—NATTUKOTTAI CHETTIARS—PRACTICE OF GUARANTEEING LOANS FROM BANKS—LOSS INCURRED AS SURETY—WHETHER BUSINESS LOSS—WHETHER ALLOWABLE DEDUCTION.

The assessee, a Nattukottai Chetti, carrying on a money-lending business in Rangoon guaranteed a loan granted by a bank in Rangoon to a Chettiar firm. As the loan was not repaid by the borrower, the assessee was called upon to make good the amount of Rs. 19,670 under his agreement of guarantee. The assessee sought to deduct this sum as a business loss when estimating his profits :

Held, *that as it was the custom among Nattukottai Chettiars to stand surety for one another when they borrowed from banks for the purpose of lending out at higher rates of interest, the sum of Rs. 19,670 must be regarded as a loss incurred by the assessee in carrying on his money-lending business and he was therefore entitled to the deduction.*

Case referred to the High Court by the Income-tax Appellate Tribunal, Bombay, under Section 66 (1) of the Indian Income-tax Act, 1922 (Act XI of 1922), as amended by Section 92 of the Income-tax (Amendment) Act, 1939 (Act VII of 1939), in Applications 66 R. A. Nos. 6 and 7 (Madras) of 1944-45 on its file for decision on the question of law mentioned in para. 5 of the statement of case: Referred Case No. 24 of 1945.

STATEMENT OF CASE.

" These two applications for reference under Section 66 (1) of the Income-tax Act are made by the Commissioner of Income-tax, Madras, and they arise out of our orders of 16th March 1944 in R.A.A. No. 300 (Madras) of 1942-43 and 14 (1) E.P.T.A.A. No. 55 (Madras) of 1942-43. The question that he has framed is :—

' Whether in the circumstances of this case, the respondent is entitled in law to the deduction of Rs. 19,670 in his assessment for 1940-41, under Section 10 (2) (xii).'

2. The facts of this case are as follows :—

The respondent, who is a Nattukottai Chettiar, stood surety for another Chettiar firm known as one S. A. RM. of Rangoon and had

to pay under that surety agreement a sum of Rs. 19,670. The respondent as well as the firm S. A. RM. had money-lending businesses, and in the course of such businesses borrowing was a necessity. In Burma, where the businesses were being carried on, it was the custom of these money-lenders to borrow money from banks. It is a recognised rule of every bank in Burma that loans or overdrafts are not allowed unless two other persons stand as surety. It is a common practice with the Chettiars to stand surety for one another and that they stand surety not for the purpose of doing any kindness to their friends, but in furtherance and in the interests of their own business. The respondent himself stood surety for several other persons in this way apart from the said S. A. RM. firm. Similarly, he himself had to borrow money on the surety of others, which included surety of S. A. RM. for the purpose of carrying on his business. These facts had all been found by the Appellate Assistant Commissioner and there was no dispute before us either.

3. The firm of S. A. RM. borrowed money from the Chartered Bank in Rangoon and the respondent, as was the custom amongst them, stood surety. The said firm in the end failed to repay the sum of Rs. 19,670 to the Chartered Bank who realised the money from the respondent. The respondent claimed deduction of this sum from his assessable income. On a consideration of all the facts, we came to the conclusion that standing surety by one Chettiar money-lender in Burma was a part of his money-lending business there, and we thought that if one did not stand surety for another, then those others would never stand surety for him, with the result that the persons who did not stand surety would never be able to do any business in Burma. We, therefore, held that the money lost by him should be allowed as a deduction from his assessable income.

4. The only point that was made out on behalf of the department at the time of hearing of the appeal before us is that the decision of the Lahore High Court in *In the matter of Ishar Das Dharam Chand* [1], would govern the facts of this case and as it was held there that the loss incurred by an assessee by standing surety was not a loss which he incurred in connection with his business, the loss suffered in this case by standing surety should not also be allowed to be deducted. The facts of that case were that it was found that the assessee stood surety in order to do a good turn to his friend and it (the giving of surety) had nothing to do with his business. In the present case, we have, however, found that the facts are entirely different from that case. We came to the conclusion that standing surety was intimately connected with the carrying on of the money-lending

(1) (1925) 2 I.T.C. 12.

business in Burma. The Commissioner (the applicant) in his application for reference to the Honourable High Court has evidently given up the argument that was placed before us and is now seeking to establish that the transaction of the kind entered into by the respondent is of a capital nature within Section 10 (2) (xii) of the Income-tax Act, or that it amounted to creating or enlarging the goodwill of his business, which was also a capital asset.

5. We, however, think that a point of law does arise in this case and we, therefore, refer the following question as framed by the Commissioner to the Honourable High Court for their Lordships' opinion :—

'Whether in the circumstances of this case, the respondent is entitled in law to the deduction of Rs. 19,670 in his assessment for 1940-41, under Section 10 (2) (xii).'

The two applications, one referring to the income-tax assessment, and the other referring to the excess profits tax assessment in respect of a portion of the corresponding accounting period, are referred together, at the request of the Commissioner in his applications."

C. S. Rama Rao Sahib, for the Commissioner.

M. Subbaraya Aiyar, for the assessee.

JUDGMENT.

(Judgment of the Court was delivered by the Honourable the Chief Justice.)

The assessee is a Nattukottai Chetti who at all material times was carrying on a money-lending business in Rangoon. He guaranteed a loan granted by a bank in Rangoon to the Chettiar firm of S. A. RM. and as the loan was not repaid by the borrower, he was called upon to make good the amount, Rs. 19,670, under his agreement of guarantee. The assessee sought to deduct this sum as a loss when estimating his profits for the year of account 1939-40. The Income-tax Officer and the Appellate Assistant Commissioner refused to allow the deduction, but on appeal to the Income-tax Appellate Tribunal, the assessee's contention was accepted. The Tribunal's decision was based on a common practice among Nattukottai Chettiars. It is their custom to borrow from banks for the purpose of lending out the sums so obtained at higher rates of interest. The banks require such overdrafts to be guaranteed by other Chettiars. The Chettiars stand surety for one another in these borrowings. If a Chettiar refused to accommodate another money-lender in this way, he would not be able to obtain a guarantor for his own essential borrowings. The assessee in this case borrowed money on the guarantee of others and in turn stood surety for other Chettiars. In these circumstances, the Tribunal considered that the sum of Rs. 19,670 which the assessee was called upon to pay

fell under Section 10 (2) (xii), that is, it was an expenditure (not being in the nature of capital expenditure or personal expenses), laid out or expended wholly and exclusively for the purpose of his business.

The Commissioner of Income-tax applied to the Tribunal to state a case to this Court as he considered that this decision was wrong in law. As a result the Tribunal has referred to this Court the following question :—

"Whether in the circumstances of this case, the respondent is entitled in law to the deduction of Rs. 19,670 in his assessment for 1940-41, under Section 10 (2) (xii)."

We consider that it would be straining the language of Section 10 (2) (xii) to hold that the deduction can be made under that provision; but this does not mean that the assessee is not entitled to the deduction. Before the 1939 Amendment Act, there was no provision in the Indian Income-tax Act for the deduction of bad debts when calculating the taxable profits of the business, but of course such debts had to be deducted in order to arrive at the true figure of the profits earned. The sum of Rs. 19,670 represented a loss incurred by the assessee in carrying on his money-lending business and therefore he was entitled to the deduction. By reason of the practice among Nattukottai Chettiars to which we have referred this debt can only be regarded as a business loss.

We answer the question referred in favour of the respondent. The Commissioner of Income-tax will pay the costs Rs. 250.

Reference answered accordingly.

[IN THE LAHORE HIGH COURT.]

GULAB SINGH JOHRI MAL, *In re* (No. 1).

DIN MOHAMMAD and MEHR CHAND MAHAJAN, JJ.

October 4, 1945.

INDIAN INCOME-TAX ACT (XI OF 1922), SEC. 25-A—HINDU UNDIVIDED FAMILY—PARTITION—SUIT FOR DECLARATION THAT FAMILY HAD DISRUPTED—ARBITRATOR'S AWARD—REJECTION OF APPLICATION UNDER SEC. 25-A—LEGALITY—DATE OF PARTITION.

The assessee firm which was assessed as a Hindu undivided family consisting of a father and his sons up to 1936-37 applied in the assessment year 1936-37 under Section 25-A of the Income-tax Act stating that partition had taken place and relied on an arbitrator's award dated 1st March 1937. The application was however rejected by the Income-tax authorities for both the assessment years 1936-37 and

1937-38 and the assessee was continued to be assessed as a Hindu undivided family. On 17th August 1939 a suit was instituted by the father against his sons for a declaration that the family had disrupted on 1st March 1937 and for partition of certain property. The suit was, at the request of the parties, referred to arbitration and the arbitrator gave an award on 25th August 1939, which was made a rule of Court. Subsequently on the basis of this award an application was again made under Section 25-A in the assessment year 1939-40 which was also rejected by the Income-tax authorities on the ground that the award was fictitious :

Held, (*i*) *that so far as the alleged disruption of the family on 1st March 1937 was concerned, the Income-tax authorities were justified in coming to the conclusion that it was bogus ;*

(*ii*) *that as from 17th August 1939, when the suit was lodged by the father, the family did disrupt and consequently as from that date there was no material on which the Income-tax authorities could come to the conclusion that partition had not taken place.*

Case referred to:—

Sir Sundar Singh Majithia *v.* Commissioner of Income-tax, C. P. and U. P. [1942] (10 I.T.R. 457 ; 202 I.C. 483 ; A.I.R. 1942 P.C. 57 ; I.L.R. 1943 All. 69 ; 45 Bom. L.R. 9).

Case stated under Section 66 (2) of the Indian Income-tax Act (XI of 1922) by the Income-tax Appellate Tribunal in pursuance of the order of the High Court dated 30th March 1944: Civil Reference No. 18 of 1944.

The order of the High Court dated 30th March 1944 on the application of the assessee under Section 66 (2) of the Indian Income-tax Act was as follows:—

" This is an application for a mandamus arising out of the refusal of the Income-tax Tribunal to refer to the High Court a question arising out of the rejection by the Income-tax authorities of an application by the assessee under Section 25-A of the Income-tax Act.

The assessee in this case was a firm styled as Messrs. Gulab Singh Johri Mal and the petition in question refers to the assessment year 1939-40.

Up to 1936-37 the firm in question was assessed as a Hindu undivided family consisting of Benarsi Das and his two sons Rameshwar Das and Ishwar Das. In the assessment year 1936-37, it was contended that the family had disrupted and reliance was placed on an award dated the 1st March 1937 given by an arbitrator, Jankinath. This application was, however, rejected both for the assessment years 1936-37 and 1937-38 (both apparently made on the same day) and the

petitioners continued to be assessed as a Hindu undivided family. This decision of the Income-tax Officer was at the time accepted without appeal.

On the 17th August, 1939, a suit was instituted by Benarsi Das against his two sons, Rameshwar Das and Ishwar Das, in which it was recited that the family had disrupted on the 1st March, 1937, but that dispute was continued in regard to the partition of certain properties. It was said that the cause of action was the refusal of the defendants to accept a scheme of partition of certain properties and also the fact that the creditors and debtors were challenging the factum of partition of 1st March, 1937. The plaintiff, therefore, asked for a declaration that the father and his two sons disrupted on the 1st March, 1937, and asking for partition of certain property. This suit was at the request of the parties referred by the Court to arbitration, and an award was announced by the arbitrator on the 25th August, 1939. This award was made a rule of the Court and decreed by the Subordinate Judge on the same day.

Subsequently on the basis of this decree, an application was again made to the Income-tax Officer under Section 25-A of the Act in respect of the assessment of 1939-40, but the Income-tax Officer rejected the factum of partition holding that the award was fictitious.

On appeal the learned Appellate Assistant Commissioner maintained the decision of the Income-tax Officer on the ground that the award which was made on the 25th August, 1939, could have no material effect on the assessment under consideration for which the accounting period ended on the 25th October, 1938. He expressed no opinion on the genuineness of the partition but added that the completeness or otherwise could be examined in its true perspective at the relevant time.

An appeal to the Tribunal failed on the ground that the whole proceedings from start to finish were collusive and fictitious. The Tribunal remarked that beyond an assertion of the parties who stood to gain by the partition, they were unable to discover any other satisfactory evidence of the alleged partition.

The petitioners then applied to the Tribunal for a reference asking for certain questions of law to be referred which they formulated on the findings of fact recorded by the Tribunal. At that stage it would appear that the case was not properly presented. The Tribunal remarked that the only question of law that could arise in the case was whether the respondent (Income-tax Department) was bound in law to hold that a partition of property had taken place simply because the parties had obtained from the Court a decree (which the Tribunal

had held was based on false and collusive admissions). But the Tribunal mentioned that this was not the case of counsel and, therefore, they held that no question of law arose which could be referred to the High Court.

At that time the decision of the Privy Council in *Sir Sundar Singh Majithia* v. *Commissioner of Income-tax*[1] had not been announced. As now urged by Mr. Bajaj on behalf of the petitioners, it becomes clear that by reason of that decision a question of law does arise involving the question, whether by reason of the decree dated the 25th August, 1939, the Income-tax authorities were justified in refusing the application under Section 25-A of the Income-tax Act. On page 465 of the judgment of the Privy Council their Lordships make the following observations :—

'Section 25-A deals with the difficulty in two ways, which are explained by the rule applicable to families governed by the Mitakshara, that by a mere claim of partition a division of interest may be effected among coparceners so as to disrupt the family and put an end to all right of succession by survivorship. It is trite law that the filing of a suit for partition may have this effect.........'

Without expressing any opinion on the effect of these observations of their Lordships on the present case we would formulate the question of law that arises as follows :—

'Is there material to justify the rejection by the Income-tax authorities of the application under Section 25-A claiming that partition had taken place and refusing to record an order that the joint family property has been partitioned among the members of the family in definite portions ?'

We direct the Tribunal to state a case on this question and refer it with their opinion to this Court.

Costs will abide the event."

STATEMENT OF CASE.

" In accordance with the orders of the High Court of Judicature at Lahore dated the 30th March, 1944, under Section 66 (2) of the Income-tax Act, directing the Tribunal to refer the question of law formulated by the Court, the following statement of the case is drawn up and the question of law referred to the Court.

2. Briefly, the facts of the case are that the assessee claimed disruption of the Hindu undivided family and applied for an order under Section 25-A for the first time in connection with the 1936-37 proceedings. The assessment proceedings for the following year, *i.e.*, 1937-38, were being conducted simultaneously and the assessment orders for

(1) (1942) 10 I.T.R. 457.

both these years were passed on the same date. No specific claim under Section 25-A was made, however, in connection with the 1937-38 proceedings. It was represented by the assessee before the Income-tax Officer that the family property was partitioned between the members of the family in definite portions on the 1st March, 1937, by virtue of a private award given by one Lala Jankinath. The Income-tax Officer was told that a few days after the above-mentioned award the parties appeared before the Magistrate on the 19th March, 1937, and made a declaration to the effect that they were separate in status and estate since 1st March, 1937, and had been carrying on the business of Gulab Singh Johri Mal since that date as partners with equal shares. The Income-tax Officer held an enquiry under Section 25-A of the Income-tax Act and came to the conclusion that the alleged disruption and division of properties was a mere camouflage and not a genuine transaction. The claim was therefore rejected.

3. The claim under Section 25-A was again made in connection with the 1938-39 proceedings but the assessee was unsuccessful since the claim was based on the identical facts which had been considered in the 1936-37 order. During the assessment proceedings for the assessment year 1939-40, a fresh claim under Section 25-A was made and this time the following further facts were placed before the Income-tax Officer. On the 17th August, 1939, a suit was instituted in the Court of the Subordinate Judge, First Class, Delhi, for partition and declaration and other reliefs. The father, Benarsi Das, was the plaintiff in this suit and the two sons, Rameshwar Das and Ishwar Das, were impleaded as defendants. Three days after the filing of the plaint, an agreement was filed in Court by which the parties agreed to refer the suit to the arbitration of Mr. Sumat Prasad, Pleader, who was straightway produced in Court and a formal order referring the suit to his arbitration was made on the same day. A week later, *i.e.*, on the 25th August, 1939, the arbitrator filed his award in Court. The same day a decree was passed by the Court in accordance with the arbitrator's award. These were the facts placed before the Income-tax Officer. On examining the award by Mr. Sumat Prasad, Pleader, the Income-tax Officer found that the arbitrator had taken no steps to ascertain the assets and liabilities and the net capital employed in the business but the divisible net capital figure was ascertained on the basis of the statements made by the parties before him. The Income-tax Officer was of the opinion that this fact alone was sufficient to throw suspicion upon the genuineness of the proceedings. The assessee's claim was rejected on this ground and on the further ground that the accounting period of the assessee

for the 1939-40 assessment being the year ended 25th October, 1938, and the date of the award being the 25th August, 1939, the award relied upon could have no material effect on the assessment under consideration. An appeal was preferred to the Appellate Assistant Commissioner against the order under Section 25-A, but was unsuccessful. The Appellate Assistant Commissioner agreed with the Income-tax Officer that the entire proceedings in Court were as much of a camouflage as the earlier proceedings on the strength of which a division and separation was alleged. The assessee then came up in appeal to the Tribunal. This appeal was determined by the Tribunal's order in 25 A. A. P. A. No. 1 (Delhi) of 1940-41. The Tribunal found that the award dated 1st March, 1937, by L. Jankinath was apparently drawn up by a lawyer who made a studied effort to evade the stamp duty and avoid registration. The document was described as 'a descriptive account of the oral arrangement of the division of the properties' and according to that document certain properties were orally allotted to the father and the two sons. The assets and liabilities of the three shops at Dareeba, Chandni Chowk and Bombay were allotted to the father Benarsi Das and the immovable properties were divided among the three members of the family. Despite the alleged allocation of the business to the father, the parties made a declaration before a Magistrate on the 19th March, 1937, to the effect that all the three of them had been carrying on the business of Gulab Singh Johri Mal as partners with equal shares since the date of the above-mentioned award. The Tribunal concluded, upon the facts, that the award by Jankinath was not an award at all. The Tribunal was of the opinion that the above-mentioned document was a disingenuous device to provide evidence of partition without incurring the expense of conforming with the legal forms. It was found that this document could not be and was not intended to be filed in Court like an ordinary award. Similarly, with regard to the subsequent proceedings in Court which ultimately resulted in a decree passed on the award by Sumat Prasad, Pleader, the Tribunal came to the conclusion that the entire proceedings were a collusive affair and the alleged separation in status and estate was not intended to be acted upon. In this view the appellant's claim was rejected by the Tribunal. A reference was claimed against the above-mentioned order of the Tribunal but was refused. In pursuance of the orders of the Court the following question of law is referred to the High Court of Judicature at Lahore under Section 66 (2) of the Income-tax Act :—

'Is there material to justify the rejection by the Income-tax authorities of the application under Section 25-A claiming that

partition had taken place and refusing to record an order that the joint family property has been partitioned among the members of the family in definite portions?'

The Court in its order under Section 66 (2) has called upon the Tribunal to forward its own opinion along with the statement of the case. The opinion of the Tribunal and the material upon which the findings of fact are based are fully set out in the Tribunal's order under Section 33 which is printed in the appendix to this statement."

Kirpa Ram Bajaj, for the assessee.

S. M. Sikri and *Jindra Lal*, for the Commissioner.

JUDGMENT.

This is a case stated by the Income-tax Appellate Tribunal in pursuance of an order issued by this Court under sub-section (2) of Section 66 of the Indian Income-tax Act. The question of law propounded by and referred to this Court reads as follows:—

"Is there material to justify the rejection by the Income-tax authorities of the application under Section 25-A claiming that partition had taken place and refusing to record an order that the joint family property has been partitioned among the members of the family in definite portions?"

The facts giving rise to this reference have been fully set out in various orders made from time to time by this Court as well as by the Income-tax authorities and need not, therefore, be recapitulated. Suffice it to say that so far as the alleged disruption of the family on the 1st March, 1937, is concerned the Income-tax authorities were fully justified in coming to the conclusion that it appeared to be a bogus affair altogether. The whole aspect of the case, however, changed when on the 17th August, 1939, the father Benarsi Das instituted a suit against his sons Rameshwar Das and Ishwar Das for partition of the property held jointly by them. It is not disputed that that matter was referred to the arbitration of B. Sumat Parshad Jain, nor can it be denied that the award made by him was on the 25th August, 1939, made a rule of the Court. This being so, a conclusive evidence of disruption came into existence binding for ever the three persons concerned. They could in no circumstances wriggle out of the situation created by them nor could they plead their own fraud if the world outside relying upon the judicial proceedings referred to above treated them as separate. These proceedings, therefore, set a seal on this disruption and consequently the Income-tax authorities were not justified in ignoring them on the grounds stated by them. Even if the arbitrator had not conducted himself in a proper manner or had failed to ascertain the assets and liabilities or the net capital of the business,

the fact remains that he partitioned the business among the three coparceners and the Court gave effect to this partition. There is ample authority in support of the proposition that such conduct on the part of the coparceners conclusively establishes disruption. In the first place, as remarked by their Lordships of the Privy Council in *Sir Sundar Singh Majithia* v. *Commissioner of Income-tax* [1], members of an undivided Hindu family can legally enter into a partnership in respect of a portion of a joint property which they have partitioned among themselves. Secondly, again as observed in the same judgment at page 465, it is trite law that the filing of a suit for partition may have this effect though it may take years before the shares of the various parties are determined or partition made by metes and bounds.

We accordingly hold that as from the 17th August, 1939, when the suit by the father was lodged, the family did disrupt and consequently as from that date there is no material on which the Income-tax authorities can come to a contrary decision. The answer, therefore, to the question referred to this Court cannot but be in the negative. This would evidently apply to those assessment proceedings only which arise after the prescribed date. The Commissioner of Income-tax will pay the costs of these proceedings to the assessee.

Reference answered in the negative.

[IN THE LAHORE HIGH COURT.]

GULAB SINGH JOHRI MAL, *In re* (No. 2).

DIN MOHAMMAD and MEHR CHAND MAHAJAN, JJ.

October 4, 1945.

INDIAN INCOME-TAX ACT (XI OF 1922), SECS. 25-A, 26-A—HINDU UNDIVIDED FAMILY—PARTITION AND FORMATION OF FIRM—APPLICATION FOR REGISTRATION OF FIRM—REFUSAL—LEGALITY.

The assessee in GULAB SINGH JOHRI MAL, IN RE (No. 1) (page 239 supra) *applied for registration of the firm under Section 26-A of the Income-tax Act for the assessment year 1939-40 and filed an instrument of partnership dated 9th November, 1937. As it was found by the Income-tax Officer that there had been no genuine separation in status and in estate between the members of the family he rejected the application under Section 26-A on the ground that there could be no contractual relationship between coparceners :*

Held, *that there was material to justify the refusal by the Income-tax Officer of the application for registration under Section 26-A of the Act.*

(1) (1942) 10 I.T.R. 457 at p. 464.

Case stated under Section 66 (2) of the Indian Income-tax Act (XI of 1922) by the Income-tax Appellate Tribunal in pursuance of the order of the High Court dated 30th March, 1944 : Civil Reference No. 17 of 1944.

The order of the High Court dated 30th March, 1944, on the application of the assessee under Section 66 (2) of the Indian Income-tax Act was as follows :—

" The facts relating to this petition for a mandamus to the Income-tax Tribunal are stated in our judgment of today's date in Civil Miscellaneous No. 30 of 1942.

The point involved in this petition arises out of the refusal of the Income-tax authorities to recognise the registration of the assessee under Section 26-A of the Income-tax Act as a firm in which the individual shares of the partners have been specified by reason of the award which purports to have given effect to the disruption of the joint family with effect from the 1st of March, 1937.

The Tribunal by its appellate order had refused to recognize the disruption and in consequence held that no case for a reference could arise in regard to the application under Section 26-A.

For the reasons given in our judgment in Civil Miscellaneous No. 30 of 1942 of today's date we have formulated a question of law arising out of the application for partition under Section 25-A, and it follows that a question of law also arises in the present case which we formulate as follows :—

'Is there material to justify the refusal by the Income-tax Officer of the application for registration under Section 26-A of the Income-tax Act ?'

We direct the Tribunal to refer this question also with their opinion to this Court. The case will be heard with the reference arising out of the connected case.

Costs will abide the event."

STATEMENT OF CASE.

" In accordance with the orders of the High Court of Judicature at Lahore dated the 30th March, 1944, under Section 66 (2) of the Income-tax Act, directing the Tribunal to refer the question of law formulated by the Court, the following statement of the case is drawn up and the question of law referred to the Court.

2. The material facts have already been set out in our statement of the case in pursuance of the Court's order in Civil Miscellaneous No. 30 of 1942. That statement may be treated as part and parcel of this. For the assessment year 1939-40 a claim for registration of the firm was made under Section 26-A of the Income-tax Act based on an instrument of partnership dated the 9th November, 1937. As a result

of the finding in connection with the assessee's application under Section 25-A to the effect that there had been no genuine separation in status and in estate between the various members of the family, the application for registration under Section 26-A was rejected by the Income-tax Officer on the ground that there could be no contractual relationship between coparceners. An appeal was preferred to the Appellate Assistant Commissioner but was unsuccessful. The assessee then came up in appeal before the Tribunal. This appeal was determined by the Tribunal by its order in 26-A Reg. A. No. 1 (Delhi) of 1940-41. In view of the Tribunal's finding in 25 A. A. P. A. No. 1 (Delhi) of 1940-41, the counsel for the assessee admitted that the appeal stood to be dismissed. The Tribunal accordingly dismissed the appeal. In pursuance of the orders of the Court under Section 66 (2) the following question of law is referred to the High Court of Judicature at Lahore:—

'Is there material to justify the refusal by the Income-tax Officer of the application for registration under Section 26-A of the Income-tax Act?'

The Court in its order under Section 66 (2) has called upon the Tribunal to forward its own opinion along with the statement of the case. The opinion of the Tribunal and the material upon which the findings of facts are based are fully set out in the Tribunal's order under Section 33 read with the Tribunal's order in 25 A. A. P.A. No. 1 (Delhi) of 1940-41, which are printed in the appendix to this statement."

Kirpa Ram Bajaj, for the assessee.

S. M. Sikri and *Jindra Lal*, for the Commissioner.

JUDGMENT.

In view of the decision arrived at by us in Civil Reference No. 18 of 1944, we have no option but to answer the question propounded in the affirmative. The result is that this petition fails and is dismissed with costs.

Reference answered in the affirmative.

[IN THE FEDERAL COURT.]

GOVERNOR-GENERAL IN COUNCIL

v.

SHIROMANI SUGAR MILLS LTD. (IN LIQUIDATION).

SIR PATRICK SPENS, C.J., SIR SRINIVASA VARADACHARIAR and SIR MUHAMMAD ZAFRULLA KHAN, JJ.

March 11, 1946.

INDIAN INCOME-TAX ACT (XI OF 1922), SEC. 46 (2)—INDIAN COMPANIES ACT (VII OF 1913), SECS. 169, 171, 211, 230, 232—COMPANY IN LIQUIDATION—ASSESSMENT TO INCOME-TAX AFTER WINDING-UP

ORDER—INCOME-TAX DEBT—PRIORITY—PROCEEDINGS WITHOUT LEAVE OF COURT FOR RECOVERY OF TAX THROUGH COLLECTOR AS ARREARS OF LAND REVENUE—LEGALITY—POWER OF COURT TO RESTRAIN PROCEEDINGS—"LEGAL PROCEEDING," MEANING OF—GOVERNMENT OF INDIA ACT, 1935, SEC. 226—HIGH COURT—BAR TO EXERCISE OF ORIGINAL JURISDICTION IN MATTERS CONCERNING REVENUE.

The respondent company was ordered to be wound up by the Allahabad High Court in 1942. An order of assessment to income-tax of the profits alleged to have been made by the company in the year ending 31st May, 1940, was made in 1943. The Income-tax Officer took proceedings under Section 46 (2) of the Indian Income-tax Act for recovery of the tax as if it were an arrear of land revenue. The Official Liquidators contended that the Income-tax Officer should lodge a claim in the winding-up proceedings and that at any rate the Income-tax Officer was not entitled to commence any proceedings under Section 46 (2) without the leave of the winding-up Court:

Held, *that a proceeding by the Income-tax authorities under Section 46 (2) of the Indian Income-tax Act was a "legal proceeding" within Section 171 of the Indian Companies Act, 1913, and accordingly, before forwarding the requisite certificate under Section 46 (2) to the Collector for the collection of the arrears of income-tax as arrears of land revenue, the Income-tax Officer should have applied under Section 171 of the Indian Companies Act for leave of the winding-up Court; but the jurisdiction conferred on the Allahabad High Court by Sections 2 and 3 of the Indian Companies Act was "original jurisdiction" within the meaning of sub-section (1) of Section 226 of the Government of India Act, 1935, and inasmuch as putting into operation the machinery of Section 46 of the Income-tax Act for the collection of arrears of income-tax as arrears of land revenue was "an act done in the collection of revenue" within the meaning of the said sub-section (1) of Section 226 of the Government of India Act, the Allahabad High Court had no jurisdiction to restrain the Income-tax authorities from proceeding without the leave of the Court to recover the arrears of income-tax in accordance with the provisions of Section 46 (2) of the Income-tax Act.*

Held, *also that in the winding up of a company the Crown is not entitled to any priority, prerogative or preferential treatment except to the extent provided for in the Indian Companies Act, in particular by Sections 230 and 232.*

The decision of the Allahabad High Court reported in [1945] (13 I.T.R. 480) reversed.

Cases referred to:

Alcock, Ashdown and Co., Ltd. *v.* Chief Revenue Authority, Bombay [1923] (L.R. 50 I.A. 227; A.I.R. 1923 P.C. 138; 75 I.C. 392; 47 Bom. 742).

Bank of Bihar Ltd., Patna *v.* Secretary of State and Others [1932] (A.I.R. 1932 Pat. 1).

Best & Co., Ltd. *v.* Collector of Madras [1918] (35 M.L.J. 23; 1 I.T.C. 18; 48 I.C. 790).

Commissioner of Income-tax *v.* Official Liquidators, Agra Spinning and Weaving Mills Co. [1934] (I.L.R. 56 All. 685; A.I.R. 1934 All. 170; 152 I.C. 183; 2 I.T.R. 79).

Damagoria Coal Co., Ltd., *In re* [1931] (I.L.R. 59 Cal. 327; 2 Comp. Cas. 240; 137 I.C. 870; A.I.R. 1932 Cal. 430; I.R. 1932 Cal. 371).

Dewarkhand Cement Co. Ltd. *v.* Secretary of State [1939] (I.L.R. 1939 Bom. 320; 182 I.C. 835; 2 F.L.J.H.C. 60; 41 Bom. L.R. 297; A.I.R. 1939 Bom. 215).

Food Controller *v.* Cork ([1923] A.C. 647).

Governor-General in Council *v.* Sargodha Trading Co., Ltd. [1943] (I.L.R. 1943 Lah. 706; 208 I.C. 17; 46 P.L.R. 1; 13 Comp. Cas. 163; A.I.R. 1943 Lah. 228; 11 I.T.R. 368).

Govindarajulu Naidu *v.* Secretary of State [1927] (I.L.R. 50 Mad. 449: A.I.R. 1927 Mad. 689; 105 I.C. 576; 53 M.L.J. 355).

Hansraj Gupta and Others v. Dehra Dun Mussoorie Electric Tramways Co., Ltd. [1933] (A.I.R. 1933 P.C. 63; 3 Comp. Cas. 207).

Northern Bengal Co., Ltd. (In Liquidation), In the matter of [1936] (41 C.W.N. 458; 7 Comp. Cas. 470).

Secretary of State *v.* Punjab Industrial Bank Ltd. [1931] (I.L.R. 12 Lah. 678; 32 P.L.R. 367; A.I.R. 1931 Lah. 351; 1 Comp. Cas. 303).

Shukantla *v.* The Peoples' Bank of Northern India Ltd. (In Liquidation) [1941] (I.L.R. 1941 Lah. 760; A.I.R. 1941 Lah. 392; 197 I.C. 1; 11 Comp. Cas. 309).

Spooner *v.* Juddow (1846-50) (4 Moore's I.A. 353; 6 Moo. P.C. 257).

Webb & Co. ([1922] 2 Ch. 369).

West Laikdih Coal Co., Ltd., In the matter of [1925] (I.L.R. 53 Cal. 328; A.I.R. 1926 Cal. 781; 96 I.C. 37).

Appeal from a judgment of the Allahabad High Court reported as *Shiromani Sugar Mills Ltd.* v. *Governor-General in Council* [1945] (13 I.T.R. 480): Civil Appeal No. II of 1945.

M. C. Setalvad, Senior Advocate, Federal Court (*G. N. Joshi, Advocate, Federal Court*, with him), instructed by *K. Y. Bhandarkar, Agent*, for the appellant.

Dr. K. N. Katju, Senior Advocate, Federal Court (*S. S. Dhawan, Advocate, Federal Court*, with him), instructed by *Naunit Lal, Agent*, for the respondent.

JUDGMENT.

The judgment of the Court was delivered by

SPENS, C. J.—The respondent company prior to being wound up, as hereinafter mentioned, carried on the business of proprietors of sugar mills in the Basti District of the United Provinces. The company was believed to have made some profits for the year ending the 31st May, 1940, but it was not until the 25th of February, 1943, that an order for assessment of income-tax was made for the year of assessment 1941-42, and the tax was eventually fixed at Rs. 18,493-12-0. In the meantime, however, a petition to wind up the company had been presented on the 26th of November, 1941, a provisional liquidator had been appointed on the 7th of December, 1941, and finally, on the 17th

of April, 1942, a winding-up order had been made by the High Court at Allahabad. It will be noticed therefore that the company had been ordered to be wound up a very considerable time before the assessment was made. On the 10th of March, 1943, a notice of demand was served on the Official Liquidators of the respondent company under Section 29 of the Indian Income-tax Act, 1922 (hereinafter referred to as "the Income-tax Act"). On the 13th of March, 1943, the Official Liquidators pointed out to the Income-tax Department that the proper procedure to be followed was for the Income-tax Department to lodge a claim in the winding-up in respect of the arrears of tax alleged to be due from the company.

Instead of adopting the procedure suggested, the Income-tax Department decided to adopt the procedure provided by Section 46 of the Income-tax Act, and accordingly, on the 8th of August, 1944, the Income-tax Department sent an 'Arrear Demand' to the Official Liquidators with the intimation that the demand was recoverable as arrears of land revenue, and that a recovery certificate under sub-section (2) of Section 46 had been forwarded to the Collector of Allahabad. In fact, on the 10th of July, 1944, the Official Liquidators had already received from the Collector of Allahabad a demand for the recovery of the said amount of Rs. 18,493-12-0 as arrears of land revenue. In these circumstances, the Official Liquidators, having taken legal advice, made an application to the High Court under Sections 171, 228 and 233 of the Indian Companies Act, 1913, against the Governor-General in Council, through the Fourth Additional Income-tax *cum* Excess Profits Tax Officer, Excess Profits Tax Circle, Cawnpore, as respondent, asking for an order that the respondent be directed to put in a formal claim to the Official Liquidators in respect of the said sum of Rs. 18,493-12-0, and praying for an order restraining the Collector from effecting recovery of the said sum as arrears of land revenue, pending the disposal of the application. On the same day, *viz.*, the 21st of September, 1944, the Court made an interim order restraining the Collector from effecting recovery of the said sum. The application finally came before Iqbal Ahmad, C. J., and Braund, J., for argument and disposal, and on the 13th of November, 1944, judgment was delivered and a final order passed by the said learned Judges. The said order directed that under Section 169 of the Indian Companies Act, 1913, the respondent should be restrained from proceeding without leave of the Court with the subsisting proceeding before the Collector at Allahabad for the recovery of the said sum of Rs. 18,493-12-0 as an arrear of land revenue in accordance with Section 46 of the Income-tax Act, provided nevertheless that the said injunction should be without prejudice to such application, if any, as the respondent might be advised to make under

Section 171 of the Indian Companies Act, 1913, for leave to proceed with such recovery. The said order also provided that the present appellant should pay to the Official Liquidators the sum of Rs. 538-12-0 as costs.

It may be conveniently noticed here that the actual form of the order was not technically accurate. Section 169 of the Indian Companies Act, 1913, only authorises the Court to restrain proceedings, "at any time after the presentation of the petition for winding-up a company under this Act, and *before* making an order for winding-up the company." In view of the fact that the winding-up order had already been made, no injunction in this case could be granted under Section 169. No formal objection, however, was taken in regard to this matter, and it is clear from the judgment of the learned Judges that in this respect the substantial question was whether or not the appellant should have obtained the leave of the Court under Section 171 of the Indian Companies Act prior to taking steps to put into action the machinery of Section 46 of the Income-tax Act. The effect of the decision was that such leave was required, and that as it had not been obtained, the Court could restrain further action under Section 46. The learned Judges also held that the objection raised by the present appellant to the exercise by the Allahabad High Court of any jurisdiction at all in the matter based on Section 226 of the Government of India Act, 1935, was ill-founded, and that they were free to deal with the matter. They granted, however, a certificate under Section 205 of the last mentioned Act and accordingly the appellant has come to this Court, and asks that the order of the 13th of November, 1944, be set aside, both on the ground that the High Court had no jurisdiction to deal with the matter, in view of the provisions of Section 226 of the Government of India Act, 1935, and on the ground that the action taken by the revenue authorities under Section 46 of the Income-tax Act did not require any prior leave of the Court under Section 171 of the Indian Companies Act, 1913.

We propose to deal with the second question first. Section 171 of the Indian Companies Act, 1913, is in the following terms :—

"When a winding-up order has been made, or a provisional liquidator has been appointed, no suit or other legal proceeding shall be proceeded with or commenced against the company except by leave of the Court, and subject to such terms as the Court may impose."

In the High Court considerable discussion seems to have taken place as to the general position of debts due to the Crown and the prerogative rights of the Crown in a liquidation of a company under the Indian Companies Act, 1913. As the point was also raised in this Court, we think that it is desirable to dispose of that

matter before discussing the matters that more directly arise under Section 171. The necessity on behalf of the Crown of obtaining the prior leave of the Court under Section 171 is in a measure connected with the question of the extent to which the prerogative or priority rights of the Crown have been affected by the enactment of the Indian Companies Act, 1913.

In Section 230 of that Act a modified priority is expressly provided for a certain limited class of Crown debts. [See sub-section (1) (a)]. These include debts in respect of revenue, taxes, cesses and rates payable to the Crown, but the provision is limited to those due from the company at a prescribed date and having become due and payable within the twelve months next before that date, the prescribed date being the date of the commencement of the winding-up, or in the case of a company ordered to be wound up compulsorily, which has not previously commenced to be wound up voluntarily, the date of the winding-up order. Moreover, the priority expressly so given to Crown debts is not confined solely to Crown debts. They have to rank *pari passu* for payment with certain debts due to local authorities, certain debts in respect of salary or wages due to clerks, servants, labourers or workmen, compensation payable under the Workmen's Compensation Act, 1923, and other classes of debts and expenses, and all have to abate equally if the assets are insufficient to meet them in full. In this connection it is material also to notice sub-section (2) of Section 232 of the Indian Companies Act, 1913. This sub-section indicates that an express enactment was considered necessary to provide that the consequences set out in sub-section (1) of Section 232 should not apply to proceedings of the Government. To these indications of the manner in which the Crown prerogative has been expressly dealt with by the provisions of the Indian Companies Act may be added a general consideration derived from the whole scheme of the Act in regard to the administration of assets in the liquidation of companies. It is difficult to believe that where so much consideration has been given to rights of priority and the respective rights and position of secured and unsecured creditors, and the order and manner in which their debts are to be discharged, the Crown was to remain outside the scheme and unaffected by the provisions of the Act, except to the extent to which Crown rights have been expressly dealt with. It is difficult to think of any reason for qualifying the priority in respect of the Crown debts specified in Section 230 (1) (a), if it was intended that other debts due to the Crown should enjoy unqualified priority. This provision is in marked contrast to the provision contained in the Indian Insolvency Acts allowing priority in respect of "all debts due to the Crown or to

any local authority." (Presidency Towns Insolvency Act, III of 1909, Section 49; and Provincial Insolvency Act, V of 1920, Section 61). It was mainly the express provisions of Section 209 of the English Companies Act, 1908 (now re-enacted as Section 264 of the Companies Act, 1929), and this general consideration of the whole statutory administrative scheme of company's assets in a liquidation provided for in the later English Companies Acts, and the anomalies and difficulties which would ensue if the Crown were not bound thereby, that led the English Court of Appeal in *Webb & Co.*[1], and the House of Lords (affirming the above decision) in *Food Controller* v. *Cork*[2], to determine, once and for all, that the Crown is not entitled to priority in payment of its claims over, or to issue process to obtain payment in full in priority to, other creditors of a company in liquidation, except as expressly provided by Section 209 of the English Act of 1908, now Section 264 of the English Companies Act, 1929. These sections very closely resemble Section 230 of the Indian Companies Act, 1913, in so far as a very limited priority and preference is expressly given to certain Crown debts in the liquidation of a company. Having regard to the similarity of the provisions of the Indian Companies Act, 1913, to the English Acts of 1908 and 1929, in respect of the general statutory scheme of administration of a company's assets in liquidation, and to the correspondence between the provisions of Section 230 of the Indian Act with those of Section 209 or Section 264 of the English Acts, it is not surprising that later Indian decisions on the rights of the Crown in a liquidation in India have followed the reasoning of the English cases above referred to. *Cf. In re Damagoria Coal Co., Ltd.*[3]; *Secretary of State* v. *The Punjab Industrial Bank Ltd., (In Liquidation)*[4]; *Bank of Bihar Ltd., Patna* v. *Secretary of State and Others*[5]; *In the matter of the Northern Bengal Co., Ltd., (In Liquidation)*[6]; *Governor-General in Council through the Income-tax Commissioner, Punjab, N.W.F. and Delhi Provinces* v. *Sargodha Trading Co., Ltd., (In Liquidation)*[7]. Counsel for the appellant invited our attention to these cases, but did not suggest that they were in any way wrongly decided, or that the scheme of the administration of assets of a company in liquidation under the Indian Act was materially different to that enacted by the English Acts, notwithstanding the decisions to the contrary in *In the matter of West Laikdih Coal Co., Ltd.*[8], and *Commissioner of Income-tax* v. *Official Liquidators, Agra Spinning and Weaving Mills Co.*[9] We have no hesitation in coming to a conclusion and holding that the Crown is bound by the provisions of the Indian

(1) [1922] 2 Ch. 369.
(2) [1923] A.C. 647.
(3) (1931) I.L.R. 59 Cal. 327.
(4) (1931) I.L.R. 12 Lah. 678.
(5) (1932) A.I.R. 1932 Pat. 1.
(6) (1936) 41 C.W.N. 458.
(7) (1943) I.L.R. 24 Lah. 706; 11 I.T.R. 368.
(8) (1925) I.L.R. 53 Cal. 328.
(9) (1934) I.L.R. 56 All. 685; 2 I.T.R. 79.

Companies Act, 1913, and is bound, in regard to the provisions relating to the liquidation of companies, " to a statutory scheme of administration wherein the prerogative right of the Crown to priority no longer exists." (Lord Wrenbury in *Food Controller* v. *Cork*[1], at page 672). The Crown is accordingly not entitled, in our judgment, to any prerogative, priority, or preferential rights or treatment, save those expressly conferred and limited by the Act itself, in particular by Section 230 and sub-section (2) of Section 232.

Before we turn to the more detailed consideration of Section 171 of the Indian Companies Act, it may also be noted that the particular arrears of income-tax, which the appellant has endeavoured to collect through the machinery of Section 46 of the Income-tax Act, do not come within the prescribed class of taxes for which the Crown can claim even the limited priority given by Section 230 of the Indian Companies Act. Having regard to the delay in assessment, these arrears were not due from the company at the date of the winding-up order. In respect of them the Crown ranks as an ordinary unsecured creditor. None the less, the appellant claims not only that the appellant is free to exercise in this case the machinery of Section 46 of the Income-tax Act, but that also the appellant is free to collect these arrears in full without any obligation to account to the Liquidators or to bring into Court any excess above what the appellant might receive if a claim as an unsecured creditor had been made. It appears that, excepting the power of the Court under Section 171 to impose a condition at the time of granting leave, there is no machinery or provision in the Act to compel the appellant to account for or bring into Court any such excess. Accordingly, this claim to exercise the machinery of Section 46, if successful, would in effect enable the Crown to secure for the arrears set out above, the very priority to which both in England and India the Crown has been held not entitled.

Hitherto, though it may be that attempts have been made to collect arrears of income-tax due from a company in liquidation through the machinery of Section 46 of the Income-tax Act, the Income-tax authorities have, upon objection being taken by the Liquidators, submitted to prove their claim in the liquidation like any other creditor. *Cf. Governor-General in Council through the Commissioner of Income-tax, Punjab, N.W.F. and Delhi Provinces* v. *Sargodha Trading Co., Ltd.*, (*In Liquidation*)[2] above referred to. This they are now not prepared to do and the appellant presses for the sanction of the Court to be given to the right to exercise the machinery of Section 46 of the Income-tax Act in respect of arrears of income-tax due from a company

(1) [1923] A.C. 647. (2) (1943) I.L.R. 24 Lah. 706; 11 I.T.R. 368.

in liquidation uncontrolled by the Court in which the company is being wound up.

How then is this claim in fact formulated? Counsel for the appellant urges (a) that under Section 46 of the Income-tax Act, the very special machinery therein set forth is not in any way limited in its application and is *prima facie* therefore applicable to thefacts of this case and available and appropriate for the collection of arrears of income-tax due from the respondent company, whether it be in liquidation or not; (b) that the powers of the Court in a winding-up under the Indian Companies Act to control, restrain or interfere with claims or actions or remedies of creditors are very limited and are confined to Sections 169 and 171; (c) that the former section gives jurisdiction during the period only between the presentation of a petition and the making of an order for the winding-up of the company and only upon the application of a company, a creditor, or a contributory, to restrain "further proceedings in any suit or proceeding against the company upon such terms as the Court thinks fit"; and (d) that Section 171 by contrast provides that "after a winding-up order has been made or a provisional liquidator appointed, no suit or other legal proceeding shall be proceeded with or commenced against the company, except by leave of the Court and subject to such terms as the Court may impose." Counsel emphasised the difference in wording between the two sections—"any suit or proceeding" in Section 169, "no suit or other legal proceeding" in Section 171. He argued that for a proceeding to be within the scope of Section 171, it must be (i) in the nature of a suit, relying for this purpose on the words "suit or other," and the decision of a Lahore Full Bench (Tek Chand, Monroe and Beckett, JJ.) in *Shukantla* v. *The Peoples' Bank of Northern India Ltd., (In Liquidation)*[1], and (ii) a proceeding in a Court of law, in which way only could proper effect be given to the phrase "legal proceeding" as contrasted with the word "proceeding" only. The correctness of the decision in the Lahore Full Bench above referred to, namely, that a suit under Order XXI, r. 63, of the Civil Procedure Code, for a declaration of title against a company in liquidation cannot be commenced without the previous leave of the Court which has passed the winding-up order, cannot, we think, be doubted. But the observations of the learned Judges must of course be read in the light of the point before them for decision, which was a very narrow one. As a statement of law of general application, we, as were the learned Judges in the Allahabad High Court in this case, are unable to accept the narrow construction put upon the expression "or other legal proceeding" in the judgment

(1) (1941) I.L.R. 22 Lah. 760.

of the Lahore Full Bench. In our judgment, it need not, and therefore should not, be confined to "original proceedings in a Court of first instance, analogous to a suit, initiated by means of a petition similar to a plaint." Section 171 must, in our judgment, be construed with reference to other sections of the Act and the general scheme of administration of the assets of a company in liquidation laid down by the Act. In particular, we would refer to Section 232. Section 232 appears to us to be supplementary to Section 171 by providing that any creditor (other than Government) who goes ahead, notwithstanding a winding-up order or in ignorance of it, with any attachment, distress, execution or sale, without the previous leave of the Court, will find that such steps are void. The reference to "distress" indicates that leave of the Court is required for more than the initiation of original proceedings in the nature of a suit in an ordinary Court of law. Moreover, the scheme of the application of the company's property in the *pari passu* satisfaction of its liabilities, envisaged in Section 211 and other sections of the Act, cannot be made to work in co-ordination, unless all creditors (except such secured creditors as are "outside the winding-up" in the sense indicated by Lord Wrenbury in his speech in *Food Controller* v. *Cork*[1]) are subjected as to their actions against the property of the company to the control of the Court. Accordingly, in our judgment, no narrow construction should be placed upon the words "or other legal proceeding" in Section 171. In our judgment, the words can and should be held to cover distress and execution proceedings in the ordinary Courts. In our view, such proceedings are other legal proceedings against the company, as contrasted with ordinary suits against the company.

That still leaves open the question whether action under Section 46 of the Indian Income-tax Act is covered by the phrase "other legal proceeding." Clearly it is not a proceeding in an ordinary Court of law. But we see no reason why in British India no "legal proceeding" can be taken otherwise than in an ordinary Court of law, or why a proceeding taken elsewhere than in an ordinary Court of law, provided it be taken in a manner prescribed by law and in pursuance of law or legal enactment, cannot properly be described as a "legal proceeding." If it be considered that the effect of the Income-tax authorities putting the machinery of Section 46 of the Income-tax Act in motion for the collection of arrears of income-tax is to bring into operation all the appropriate legal enactments relating to the collection of land revenue in the Province concerned, it is, in our judgment, very difficult to say that they are not taking a "legal proceeding." In fact, in this very case, had the company not been in liquidation,

(1) [1923] A. C. 647 at p. 671.

the appellant would have had the choice at his option of (a) proceeding by "suit" in the ordinary Courts in respect of the arrears, or (b) by forwarding [under Section 46 (2) of the Income-tax Act] to the Collector the requisite certificate, initiating and putting into force collection of the arrears as arrears of land revenue under and in accordance with the appropriate provisions of the U. P. Land Revenue Act (III of 1901). Surely such last mentioned action on the part of the Income-tax authorities would be the adoption of another legal proceeding for the collection of the arrears as opposed to the institution of a suit. The proviso to Section 46 (2) empowers the Collector, if he so chooses, to exercise all the powers which a Civil Court may exercise in respect of the attachment and sale of debts due to a judgment-debtor. If the Income-tax Officer will be taking a "legal proceeding" when he moves the Collector—as we think he must be held to do—to realize the tax by attachment and sale of debts due to the assessee, it can make no difference in principle that the Collector is asked to exercise his summary powers under the land revenue law.

Accordingly, we agree with the learned Judges of the Allahabad High Court in holding that the words "other legal proceeding" in Section 171 of the Indian Companies Act, 1913, comprise any proceeding by the revenue authorities under Section 46 (2) of the Indian Income-tax Act, and that accordingly before forwarding the requisite certificate under Section 46 (2) to the Collector, which would put the machinery for the collection of the arrears of income-tax as arrears of land revenue into motion, the appellant should have applied in the liquidation under Section 171 of the Companies Act for leave of the winding-up Court.

That leaves the question whether, inasmuch as the appellant moved under Section 46 (2) without prior leave of the Court, the High Court at Allahabad, as the Court having jurisdiction under the Indian Companies Act to wind up the respondent company, had jurisdiction to interfere by injunction or otherwise to prevent the completion of the collection of the arrears of land revenue. Were it not for the provisions of Section 226 of the Government of India Act, 1935, we should without hesitation answer this question in the affirmative and dismiss this appeal. Section 226 must however be considered in the light of decided cases and of the facts of this case. The section runs as follows :—

"(1) Until otherwise provided by Act of the appropriate legislature, no High Court shall have any original jurisdiction in any matter concerning the revenue, or concerning any act ordered or done in the collection thereof according to the usage and practice of the country or the law for the time being in force.

(2) A Bill or amendment for making such provision as aforesaid shall not be introduced into or moved in a Chamber of the Federal or a Provincial Legislature without the previous sanction of the Governor-General in his discretion or, as the case may be, of the Governor in his discretion."

The first point to be determined is whether the section applies to the jurisdiction exercised by the Allahabad High Court under the Indian Companies Act at all. This mainly depends upon the construction to be given to the words "any original jurisdiction." Counsel for the appellant submitted that "original" was used in distinction to "appellate," and that the word "any" covered all jurisdiction over proceedings of any kind which commence and originate in the High Court. He instanced the extraordinary original jurisdiction of the Court under Clause 9 of the Letters Patent, the jurisdiction in respect of infants and lunatics under Clause 12, the ordinary original criminal jurisdiction under Clause 15, the testamentary and intestate jurisdiction under Clause 25, and the matrimonial jurisdiction under Clause 26 of the Letters Patent. He accordingly submitted that various types of original jurisdiction were conferred on the High Court by the Letters Patent, and that original jurisdiction could equally well be conferred by any valid enactment and that original jurisdiction had in fact been conferred by Sections 2 and 3 of the Indian Companies Act, 1913, on the Allahabad High Court in respect of companies whose registered offices are situate within the territorial jurisdiction of that Court. On the other hand, counsel for the respondent stressed the well-known origin and history of this section (See *Best & Co., Ltd.* v. *Collector of Madras* [1], *Govindarajulu Naidu* v. *Secretary of State* [2] and *Dewarkhand Cement Co., Ltd.* v. *Secretary of State* [3]), and asked us to construe it as a section "with an ancestral history" (See *Hansraj Gupta and Others* v. *Dehra Dun Mussoorie Electric Tramway Co., Ltd.*[4]), and to confine the meaning of the words "original jurisdiction" to the original jurisdiction exercised by the Supreme Courts and by the High Courts of Madras, Calcutta and Bombay, as successors to the Supreme Courts, and to hold that High Courts, other than those three, though they may exercise special or particular jurisdiction conferred on them by Letters Patent or statute, exercised no original jurisdiction within the meaning of the words as used in Section 226. In our opinion, the history itself of the section does not justify such a method of construction. It was clearly re-enacted in Section 106 (2) of the Government of India Act, 1915, in a setting where it was impossible to confine its operation to the High Courts of Madras, Calcutta and Bombay [*vide* Section 106 (1)], and where [*vide* Section 101 (5)] the High Court at

(1) (1918) 35 M.L.J. 23, at p. 26.
(2) (1927) I.L.R. 50 Mad. 449.
(3) (1939) I.L.R. 1939 Bom. 320.
(4) (1933) A.I.R. 1933 P.C. 63, at p. 65.

Allahabad was expressly referred to amongst the High Courts. In the Government of India Act, 1935, the very opening words of Section 226 and sub-section (2) thereof show that it is no mere repetition of a section without consideration. It has again been deliberately re-enacted with appropriate provision for its repeal or modification having regard to the changes in the constitution. We note too that the Allahabad Letters Patent in Clause 30 refer to "any final judgment, decree or order made in exercise of original jurisdiction." That orders in company matters do not differ in substance from decrees in suits, is shown by Section 199 of the Indian Companies Act providing that such orders shall be enforced in the same manner in which decrees in a suit may be enforced. The present order of the High Court is thus in effect a decree in a suit granting an injunction. We are accordingly unable to accept the argument on behalf of the respondent and feel bound to hold that Section 226 applies to the jurisdiction conferred on the Allahabad High Court by the Indian Companies Act, 1913.

It was suggested on behalf of the respondent company that the opening words "until otherwise provided by Act of the appropriate legislature" need not necessarily be confined to future legislation, and that if the Indian Companies Act had in fact "provided otherwise," the section would not apply to jurisdiction exercised under the Indian Companies Act. In our judgment, this construction also cannot be maintained. Reading the two sub-sections of Section 226 together, in our judgment, that which is contemplated is future legislation enacted in accordance with the changes in the constitution. So far there has been no such legislation, either by way of repeal or modification. The section with all its anomalies, so constantly commented upon by High Court after High Court and before now by this Court, remains on the Statute Book. Once again, we point out this anomalous situation that if a District Court, such as the District Court at Cawnpore, upon which jurisdiction under the Companies Act of 1913 has been conferred under the proviso to Section 3 (1) of the Act, had been dealing with this claim of the Crown, or the matter had come before the High Court itself in its appellate jurisdiction, neither the District Court nor the High Court would have had to consider Section 226. But so long as the section remains on the Statute Book, it is our duty to give to it what we consider to be its true effect, however capricious that may be.

The next two points which require consideration are :—

(a) Did the High Court purport to exercise jurisdiction in a matter concerning the revenue or concerning any act ordered or done in the collection thereof; and

(b) if so, do the last words of the sub-section "according to the usage and practice of the country or the law for the time being in

force" qualify "original jurisdiction in any matter concerning the revenue" as well as "concerning any act ordered or done in the collection thereof?"

As regards (a), there was much discussion before us in this case, as there had been in other cases, whether a matter concerning an act ordered or done in the collection of the revenue would not also be included in a matter concerning the revenue, or whether it would not be something additional to or different from a matter concerning the revenue. In *Dewarkhand Cement Co., Ltd.* v. *Secretary of State*[1] the learned Judge (Rangnekar, J.) basing himself on an observation in the judgment delivered by Lord Phillimore in *Alcock, Ashdown and Co., Ltd.* v. *Chief Revenue Authority, Bombay*[2], came to the conclusion that two different ideas are expressed in the respective parts of the section; the first refers to the preliminary proceedings taken for the purpose of determining the amount of the revenue in any case, and the second to the machinery to enforce payment of the revenue so determined. Another view suggested in the course of the hearing before us was that all claims directly in respect of revenue by or against the Crown would be matters concerning the revenue, whereas claims against individual officials in respect of acts ordered or done in the collection of the revenue might not be included in matters concerning the revenue and that accordingly the latter words had to be added for the protection of officials and to prevent indirect attacks upon the revenue. It is not, in our judgment, necessary to come to any final conclusion on these views. On the facts of this case, we are satisfied that by reason of the making out and forwarding to the Collector of a certificate in the form and manner prescribed by Section 46 (2) of the Income-tax Act, thereby putting into operation the machinery of Section 46 for the collection of the arrears of income-tax in question as arrears of land revenue, an act was done in the collection of the revenue, and in granting the injunction in this case the High Court was exercising original jurisdiction in a matter concerning an act done in the collection of the revenue.

As regards (b), we are satisfied that grammatically the last words of the sub-section in question can only qualify the words immediately preceding, "concerning any act ordered or done in the collection thereof."

That brings us to the last and final point of construction. Was the action of the appellant which is challenged in this case an act done in the collection of the revenue "according to the usage and practice of the country or the law for the time being in force?" It

(1) (1939) I.L.R. 1939 Bom. 320. (2) (1923) L.R. 50 I.A. 227.

was not suggested that the usage or practice of the country comes into this case. The question to be determined is, was the action of the appellant in the collection of the revenue "according to the law for the time being in force" within the true meaning to be given to these words in the light of the facts of this case and decided cases. The learned Judges in the Allahabad High Court were able to come to their conclusion in favour of the respondent on the ground that what the appellant did in this case was contrary to the law for the time being in force, in the sense of all the law applicable to the matter, including the Indian Companies Act, 1913. An attempt has been made to collect arrears from a company in liquidation by a procedure not authorised by law generally. Accordingly, they say, the matter is outside the limitations to jurisdiction imposed by Section 226. It has been urged on behalf of the appellant that the learned Judges were wrong in allowing the phrase "law for the time being in force" to embrace all law for the time being in force in respect of the act ordered or done in the collection of the revenue, and that they should have confined the phrase to law directly concerned with the collection of the revenue. We are not prepared to differ in this respect from the learned Judges in the Court below. It would be difficult, if not impossible, to delimit satisfactorily the law which had to be considered in relation to any matter from that which could be excluded from consideration. But in our view the more important question in this case is whether the act ordered or done in the collection of the revenue must in truth and in fact have been "according to the law for the time being in force," or whether it is sufficient that the person or persons ordering or doing the act should *bona fide* and not absurdly have believed that the act was "according to the law for the time being in force." Counsel for the appellant pressed us with the view that the latter only was sufficient to bring this case within Section 226 (1), and he relied upon the well-known case of *Spooner* v. *Juddow*[1]. The learned Judges in the Court below were able to come to the conclusion that the principles of *Spooner* v. *Juddow*[1] did not apply when the complaint was that the whole procedure was not according to the law for the time being in force, or that the revenue authorities had no legal power to do what they had done, as opposed to complaint of some irregularity in carrying out procedure authorised by law or an irregularity in doing something which they had power to do. We regret that with respect we feel bound to differ from the learned Judges in their limited view of the application of the principles of *Spooner* v. *Juddow*[1]. On the facts of that case, we doubt if

(1) (1846-50) 4 Moore's I.A. 353.

the officials were only guilty of a mere irregularity of procedure. But be that as it may, it seems to us that there is really no difference in principles between the case of an official believing *bona fide* and not absurdly that some illegal step which he takes in executing a legally authorised procedure is itself according to the law for the time being in force, and that of another official believing *bona fide* and not absurdly that the procedure which he adopts in a particular case is itself according to the law for the time being in force. The following passage from the opinion delivered by Lord Campbell at pages 379-80 appears to us to apply as much to one such *bona fide* mistake as to the other :—

"The point, therefore, is, whether the exception of jurisdiction only arises where the defendants have acted strictly, according to the usage and practice of the country, and the regulations of the Governor and Council. But upon this supposition the proviso is wholly nugatory; for if the Supreme Court is to inquire whether the defendants in this matter concerning the public revenue were right in the demand made, and to decide in their favour only if they acted in entire conformity to the regulations of the Governor and Council of Bombay, they would equally be entitled to succeed, if the statutes and the charters contained no exception or proviso for their protection. Our books actually swarm with decisions putting a contrary construction upon such enactments, and there can be no rule more firmly established, than that if parties *bona fide* and not absurdly believe that they are acting in pursuance of statutes and according to law, they are entitled to the special protection which the legislature intended for them, although they have done an illegal act. In this case it may well be that the warrant against the goods of *Tookaydass* did not authorize the taking the goods of *Hurgovundass*, or even that *Hurgovundass* might not be liable for the arrears of 'quit-rent' which accrued before he became owner of the house. Still the Collector was evidently of opinion, that a distress might be made for the whole of the arrears due, and that it was sufficient to introduce into the warrant the name of *Tookaydass*, in whose name the house continued to be registered. The other defendant never could have doubted the sufficiency of the warrant. If Indian revenue-officers have fallen into a mistake, or without bad faith have been guilty of an excess in executing the duties of their office, the object of the legislature has been, that they should not be liable to be sued in a civil action before the Supreme Courts. Liability to be prosecuted criminally, stands upon a totally different foundation."

If accordingly we are of opinion that the certificate prescribed by Section 46 (2) was made out and forwarded to the Collector under that

sub-section by officials *bona fide* and not absurdly believing that the machinery under Section 46 was legally proper and available for the collection of the arrears of income-tax in question due from the respondent company, we must conclude that Section 226 (1) applies to this case, and that in granting the injunction appealed against the High Court was purporting to exercise original jurisdiction concerning an act ordered or done in the collection of the revenue *bona fide* and not absurdly believed to be according to the law for the time being in force, and that by reason of Section 226 (1) and the decision in *Spooner* v. *Juddow*[1], the High Court had no jurisdiction in the matter, and their order was *ultra vires* and void.

Now so far as the facts of this case on the record are concerned, it is not absolutely clear on which date the certificate under Section 46 (2) of the Income-tax Act was made out and forwarded to the Collector. The first intimation which the Liquidators received that the Section 46 procedure was going to be adopted was the receipt on the 10th July, 1944, of the demand from the Collector for the recovery of the arrears as arrears of land revenue. This was fully explained to the Liquidators by a letter from the Income-tax Department of the 8th August, 1944, which made clear that a certificate had been forwarded to the Collector under Section 46 (2). It is true that these steps were taken more than a year after the Liquidators had suggested that the proper course for the Income-tax Department was to lodge a claim in the liquidation. But on those facts it is difficult to suggest that in July and August 1944, the Income-tax authorities were not acting *bona fide*, or were acting absurdly in determining to proceed under Section 46 (2). Nor has anyone suggested anything of that sort in this case. It is also true that in the other similar cases the Income-tax Department had previously submitted to lodge claims for arrears claimed due from a company in liquidation in the liquidation. But it still is not impossible that a perfectly *bona fide* and not absurd determination was come to in this case to try to recover the arrears by a procedure believed to be available to the Income-tax authorities according to their view of the law for the time being in force. Indeed the number of points raised and debated before us and the High Court show that it would be very difficult to hold that the challenged procedure had clearly been adopted *mala fide* or absurdly. At the stage therefore when the procedure which we have held to be unauthorised by law was in fact put in force in this case, we can see no reason for holding that the officials concerned were not acting *bona fide* or were acting absurdly.

In this case, on the facts, the appellant must in our judgment succeed on the plea that Section 226 (1) of the Government of India Act,

(1) (1846-50) 4 Moore's I. A. 353.

1935, deprived the High Court of jurisdiction in the matter. Any further action under Section 46 (2) of the Income-tax Act in the future will be taken in the light of this judgment and may well not be saved by the provisions of the said Section 226.

The appellant fails on all points except the objection taken under Section 226 of the Government of India Act, 1935. By reason of that we must allow the appeal and declare that the order of the High Court of the 13th November, 1944, must be set aside, and that in lieu thereof there shall be substituted an order dismissing the application of the Liquidators of the 21st September, 1944, and directing repayment by the Liquidators of the sum, if any, received for costs in respect of the said application in the High Court, but without any further order as to costs. We make no order as to costs in respect of this appeal to this Court. *Appeal allowed.*

[IN THE CHIEF COURT OF OUDH.]

RAJA MUSTAFA ALI KHAN

v.

COMMISSIONER OF INCOME TAX, U.P. AND C.P.

MADELEY and MISRA, JJ. August 24, 1945.

INDIAN INCOME-TAX ACT (XI OF 1922), SEC. 66-A—CIVIL PROCEDURE CODE (V OF 1908), SECS. 109, 110—APPEAL TO PRIVY COUNCIL—INCOME FROM FOREST TREES, MALIKANA AND ANNUITIES—WHETHER AGRICULTURAL INCOME—LIABILITY TO INCOME-TAX—SUBSTANTIAL QUESTIONS OF LAW.

The question whether income from "malikana" and income from forest trees were agricultural income and the question whether certain payments of annuity with interest were liable to income-tax involve substantial questions of law within the meaning of Section 110 of the Civil Procedure Code.

Their Lordships accordingly granted leave to appeal to the Privy Council against the decision of the Oudh Chief Court reported as RAJA MUSTAFA ALI KHAN *v.* COMMISSIONER OF INCOME-TAX, U. P. & C. P. [1945] (13 I.T.R. 98).

Applications for leave to appeal to the Privy Council: P.C. Appeals Nos. 19 to 22 of 1944.

R. B. H. K. Ghose, for the Commissioner.

S. C. Das, for the assessee.

ORDER.

This order will cover four applications under Section 66-A (2) of the Indian Income-tax Act. Nos. 19 and 22 of 1944 are applications made by the assessee whose estate is under the Court of Wards. The

Income-tax Commissioner has also applied for leave and his applications are Nos. 20 and 21. Applications Nos. 19 and 20 relate to the assessment year 1939-40. Applications Nos. 21 and 22 relate to the assessment year 1940-41. In the first two applications we are concerned with an order of this Court dated the 29th September, 1944, in Civil Reference No. 10 of 1942. In the second two applications we are concerned with an order of this Court dated the 9th October, 1944, in Civil Reference No. 3 of 1944.

Three questions were involved :—

(1) Whether income from "malikana" is liable to income-tax,

(2) Whether income from forest is liable to income-tax, and

(3) Whether certain payments of annuity with interest were liable to income-tax.

In Nos. 19 and 20 the value of the disputed items is		
Forest	...	Rs. 21,040
Malikana	...	,, 6,271
Annuity and interest	...	,, 61,797
In Nos. 21 and 22 the items are		
Forest	...	Rs. 9,336
Malikana	...	,, 3,718
Annuity and interest	...	,, 70,365

On all these three questions this Court agreed with the Appellate Tribunal.

Section 66-A (3) provides: "The provisions of the Code of Civil Procedure, 1908, relating to appeals to His Majesty in Council shall, so far as may be, apply in the case of appeals under this section in like manner as they apply in the case of appeals from decrees of a High Court."

The valuation of the appeals cannot be directly estimated as in the case of some civil appeals, but we think that these applications properly come under Section 109 (a) as the final order involves a sum of money in each case of over Rs. 10,000. In the case of the annuity in respect of which the Income-tax Department has applied the annual payment is Rs. 1,45,862. The assessee applies for permission to appeal in respect of the sale price of forest produce and so-called malikana. The malikana is fixed for each village once for all and is payable to the Utraula estate for ever. Income-tax leviable upon the sale price of forest produce varies from year to year, but it is obvious that it must in the aggregate amount to a very large sum of money.

As we agreed with the Income-tax Tribunal on all the questions involved there must be, under Section 110, Civil Procedure Code, some substantial question of law involved. In our opinion substantial questions of law are involved in all the three matters concerning which permission to appeal has been sought.

The decision regarding "malikana," though it depends particularly upon historical considerations, raises an important question as

to what is to be considered agricultural income. The decision regarding the annuity raises an important question of income-tax law which, so far as we are aware, has not been decided by their Lordships of the Privy Council. The question whether income derived from self-grown forests is agricultural income within the meaning of the Act is obviously one of very great importance to the Government and the public and is by no means free from difficulty.

In view of these considerations we allow these four applications for leave to appeal to the Privy Council.

Applications allowed.

[IN THE PATNA HIGH COURT.]

GOVERNMENT OF BIHAR *v.* MOTIHARI ESTATE LTD.

FAZL ALI, C. J., MANOHAR LALL and SINHA, JJ.

January 9, 1946.

BIHAR AGRICULTURAL INCOME-TAX ACT (VII OF 1938), SECS. 7 (1) (a) & (b), 17 (3)—RETURN—REVISED RETURN—OPTION UNDER SEC. 7 (1) —WHETHER CAN BE EXERCISED AFTER FILING RETURN BUT BEFORE ASSESSMENT.

The assessee filed a return on 14th November, 1941, in respect of his agricultural income for the year ending 31st July, 1940, based upon the actual receipts and expenditure in the accounting period. On 26th May, 1941, the Income-tax Officer served a notice on him to submit accounts and other evidence in support of his return. Before the service of this notice, the assessee put in an application dated 23rd May, 1941, stating that the return already filed should be treated as cancelled and that he should be assessed under Section 7 (1) (a) of the Act. The Income-tax Officer assessed him under Section 7 (1) (b) on the ground that, as he had already exercised his option in submitting the original return, he could not be allowed to change the basis:

Held, *that by filing the return on 14th November, 1941, the assessee did not exercise the option under Section 7 (1) and that as under Section 17 (3) he could file a revised return before making the assessment, he was entitled to insist by the revised return that he should be assessed under Section 7 (1) (a) of the Act.*

Statement of Case under Section 25 (2) of the Bihar Agricultural Income-tax Act (VII of 1938) by the Board of Agricultural Income-tax, Bihar. Miscellaneous Judicial Case No. 112 of 1942.

STATEMENT OF CASE.

" Case stated under Section 25 (2) of the Bihar Agricultural Income-tax Act (VII of 1938) at the instance of the Motihari Estate,

Limited, Champaran, hereinafter called the assessee, referring a question of law arising from the order on his appeal against assessment for the year 1940-41.

2. The assessee while submitting his return under Section 17 (1) of the Act on 14-2-41, exercised the option allowed under sub-section (1) of Section 7 preferring to be assessed under clause (b) of that section on the basis of the actual receipts and expenditure in the accounting period 1940-41. As the return was not found to be correct and complete, a notice under Section 18 (2) of the Act was served on the assessee on 26th May, 1941, for submitting accounts and other evidence on 10-6-41 in support of his return. But before receiving this notice the assessee changed his mind and submitted another return with a written declaration, dated the 23rd/24th May, 1941, claiming to be assessed under Section 7 (1) (a) of the Act. This was not allowed and his total income was determined on the basis of the original return based on the balance sheet and the profit and loss account exhibited by him. The Agricultural Income-tax Officer, Muzaffarpur, by his order, dated the 21st June, 1941 (copy enclosed Exhibit 'C'), assessed his total income as Rs. 1,95,068 under Section 18 (3) of the Act. Against this the assessee preferred an appeal (copy enclosed Exhibit 'D') to the Commissioner of Agricultural Income-tax, Muzaffarpur, under Section 22 of the Act mainly on the grounds set forth below :—

(*i*) That the income of the assessee should have been computed according to the provisions of Section 7 (1) (a), and not under Section 7 (1) (b), and on this point the Agricultural Income-tax Officer was wrong in his interpretation of the provisions of Section 17 (3) of the Act;

(*ii*) That the sum of Rs. 825-12-0 out of the interest paid to Messrs. Daulat Ram Raut Mull, on sums borrowed for the purpose of deriving agricultural income, should not have been disallowed by the Agricultural Income-tax Officer;

(*iii*) That the Court expenses being expenses necessary for producing, maintaining and collecting the agricultural income should have been allowed by the Agricultural Income-tax Officer.

3. The assessee was heard by the Commissioner and his appeal was admitted on the last point only and the case was remanded for revising the assessment accordingly—*vide* the Commissioner's appellate order, dated the 27th January, 1942 (copy enclosed Exhibit 'T'). The assessee's total assessable income was thus reduced from Rs. 1,95,068 to Rs. 1,94,465. The assessee not being satisfied with the appellate order filed two petitions both dated the 24th March, 1942, to the Board of Agricultural Income-tax (copies enclosed Exhibits 'E and V'), one under Section 24 and another under

Section 25 of the Act for revision of the Commissioner's order on the remaining two points (i) and (ii) cited in the preceding paragraph with an alternative prayer that the first point be referred to the High Court for decision if it is not decided by the Board in his favour.

4. As held by the Board, the first point arises out of the interpretation of Section 7 of the Act. This section provides that the agricultural income shall, at the option of the assessee, (i) be deemed for purposes of assessment to be multiple of the rent of the land or of the cess-valuation of the land, or (ii) be assessed on the net amount of the income determined in the prescribed manner. The assessee filed the original return preferring to be assessed by the method contemplated in Section 7 (1) (b), but before the assessment was actually made he filed another return claiming to be assessed by the method described in Section 7 (1) (a). As it involves a question of law whether the assessee was entitled to exercise his option twice before assessment, the Board refers this question to the High Court for decision.

5. The Board is of opinion that although the Act is silent on the point the assessee after having once exercised the option allowed under Section 7 (1) by asking to be assessed under clause (b) of that section when filing his original return under the provisions of Section 17 (1) cannot be allowed to resile from this option at a later stage by claiming to be assessed under clause (a) of Section 7 (1) and file a fresh return accordingly before the assessment is actually made. The Act gives one option, not two.

6. The Board was unable to make the reference within the sixty days prescribed by Section 25 (2) for the following reasons. The application above originally filed was incomplete, and by the time it was completed the Commissioner of Agricultural Income-tax, against whose order the application was filed, had become member of the Board of Agricultural Income-tax and the case had to wait for 5 months till the return of the present member.

A copy of the Board's order is also enclosed (Exhibit 'K')."

The Advocate-General, for the Government of Bihar.

S. N. Bose and *Rai T. N. Sahay*, for the assessee.

JUDGMENT.

MANOHAR LALL, J.—This is a reference under Section 25 (2) of the Bihar Agricultural Income-tax Act—hereinafter called the Act—by the Board of Agricultural Income-tax, Bihar—hereinafter called the Board—to this Court at the instance of the assessee to answer the contention that " the income of the assessee should have been computed according to the provisions of Section 7 (1) (a), and not under Section 7 (1) (b), and on this point the Agricultural Income-tax Officer was

wrong in his interpretation of the provisions of Section 17 (3) of the Act."

The undisputed facts are these. For the year of assessment 1940-41 the assessee filed a return on the 14th of November, 1941, before the Agricultural Income-tax Officer in respect of his agricultural income for the year ending 31st July, 1940. The income returned was Rs. 1,35,088 and was based upon the actual receipts and expenditure in the accounting period. A balance sheet as on 31st July, 1940, showing the revenue and profit and loss account for this year prepared by the incorporated accountants was also filed. On the 26th May, 1941, a notice was served by the Income-tax Officer on the assessee to submit accounts and other evidence in support of his return as the officer was not satisfied that the return was correct and complete. The assessee instead of submitting the accounts filed an application stating that he should be assessed under Section 7 (1) (a). This provision enacts that "the agricultural income mentioned in sub-clause (2) of clause (a) of Section 2 shall, at the option of the assessee, be deemed, for the purposes of assessment to agricultural income-tax, to be a multiple" which shall not exceed six—the multiple has now been raised to eight. That application is dated the 23rd of May, 1941, and is to be found at page 13. It states that on the 13th of February, 1941, the assessee submitted a return for the assessment year 1940-41 and that the officer will kindly treat that return as cancelled and substitute the attached one in its place. It is stated further : "By virtue of the option allowed to us under Section 7 (1) of the Bihar Agricultural Income-tax Act, 1938, we hereby adopt the method of assessment as laid down under sub-section (a) of Section 7 (1). We have shown in the return the actual rent paid, and in order to arrive at the assessable income this sum will have to be multiplied by the multiple fixed for other district by the Bihar Board of Agricultural Income-tax." It will be noticed that this application was made before the service on the assessee of the notice issued by the Income-tax Officer under Section 18 (2) of the Act—the notice was served on the 26th of May requiring the assessee to submit accounts and evidence on the 10th of June, 1941. On the 3rd of June, 1941, the assessee was informed by the Income-tax Officer that as he had already exercised his option in submitting the original return, he cannot be allowed to change the basis. On the 5th of June, 1941, the incorporated accountants on behalf of the assessee wrote a letter to the Income-tax Officer, which is to be found at page 14, stating that they have been asked by the assessee to send a reply to the letter of the 3rd of June, 1941. The accountants after drawing attention to Section 17 (3) of the Act, which gives the assessee every right to make a revised return or a fresh return

before the assessment is made, requested the Income-tax Officer to accept a fresh return filed by the assessee. The Income-tax Officer did not agree and proceeded to make an assessment based on the original return and found out the actual amount of agricultural receipts. By an order dated the 21st of June, 1941, the assessable income was fixed at Rs. 1,95,068.

Against this assessment the assessee preferred an appeal to the Commissioner of Agricultural Income-tax, who by an order dated the 27th January, 1942, reduced the assessment to Rs. 1,94,465. The assessee then preferred two applications to the Board on the 24th March, 1942. He prayed that the order of the Commissioner be revised *inter alia* on the ground that the assessee should have been assessed under Section 7 (1) (a) and not under Section 7 (1) (b) of the Act. By the second petition it was prayed that the question of law should be referred to the High Court for decision. On the 10th October, 1942, the Board came to the conclusion that there was a question of law whether the assessee was entitled to exercise his option twice before the assessment, and that this question would be referred to the High Court. That question accordingly has been referred to this Court. There were two other minor questions which were disposed of by the Board and no reference has been made to this Court.

In my opinion the assessee was entitled in the circumstances stated above to insist that he should be assessed under Section 7 (1) (a) of the Act. Section 17 (3) is clear and allows the assessee to file a return, if he has not filed it already, or to file a revised return, if he has filed a return already, provided the assessment has not been made by that time. It is provided clearly in that clause that "any return so made shall be deemed to be made in due time under this section." It is admitted that at the time when the assessee filed his second return on the 23rd May, 1941, the assessment had not been made. The assessee, therefore, was within his right to insist by the revised return that he should be assessed under Section 7 (1) (a) of the Act.

It is argued on behalf of the Department that the assessee had already exercised his option inasmuch as he filed a return in which he showed the figures of the actual receipts in the previous year, and, therefore, he cannot be allowed to change the option already made. But I do not see that the assessee had made any such option. All he did was to file a return in which he put down certain figures as the amount of agricultural income received by him in the previous year. When the Income-tax Officer did not accept the return as correct and the assessee was asked to produce evidence in support thereof, the assessee then exercised his option by stating that the accounts need not be produced as he preferred to be assessed under Section 7 (1) (a) and he furnished material to that effect in the return.

For these reasons I would answer the question in the affirmative namely that the income of the assessee should have been computed according to the provisions of Section 7 (1) (a) of the Act and that on this point the Agricultural Income-tax Officer was wrong in his interpretation of the provisions of Section 17 (3) of the Act.

As the assessee has succeeded in his contention, he is entitled to the costs of this Court: hearing fee Rs. 150. The assessee will also be entitled to the refund of Rs. 100 which has been deposited with the Board.

FAZL ALI, C. J.— I agree.

SINHA, J.—I agree. *Reference answered accordingly.*

[IN THE BOMBAY HIGH COURT.]

VISSONJI SONS AND CO.

v.

COMMISSIONER OF INCOME-TAX, CENTRAL.

BEAUMONT, C. J., and CHAGLA, J. September 23, 1943.

INDIAN INCOME-TAX ACT (XI OF 1922), SEC. 10 (2) (xi)—BAD DEBT —MONEY LENDING BUSINESS—TWO FIRMS WITH SAME PARTNERS CARRY ON MONEY-LENDING AND MANAGING AGENCY BUSINESSES— MONEY OWED TO MANAGING AGENTS BY COMPANY WRITTEN OFF AS BAD DEBT—WHETHER AMOUNT ADVANCED IN ORDINARY COURSE OF MONEY-LENDING BUSINESS—QUESTION OF FACT—WHETHER ALLOWABLE DEDUCTION—NATURE OF FIRM.

A firm has no existence independently of its partners. If there are two firms consisting of exactly the same partners, the real position in law is that there is only one firm. It may carry on separate businesses in different names but in fact there is only one firm.

The assessee firm, Vissonji Sons & Co., were carrying on money-lending business. Another firm, Mathuradas Vissonji & Co., in which the partners were the same persons as in the assessee firm, were the managing agents of a company. The company owed the managing agents a large amount of money and a sum of Rs. 7,20,000 was voluntarily given up by them in the scheme of reconstruction of the company. It was found that no interest was charged on the loan and no other advance was made by the assessee in the ordinary course of their money-lending business in similar circumstances. The Income-tax Appellate Tribunal held that the sum of Rs. 7,20,000 was not money advanced by the assessee in the ordinary course of their money-lending business and it could not therefore be claimed as a bad debt under Section 10 (2) (xi) of the Income-tax Act:

Held, *that the only question of law that arose was whether there was any evidence to justify the finding of fact by the Tribunal and that there was ample evidence to justify the finding.*

Reference under Section 66 (1) of the Indian Income-tax Act (XI of 1922) by the Income-tax Appellate Tribunal: Income-tax Reference No. 2 of 1943.

STATEMENT OF CASE.

" These four applications are made by the firm of Vissonji Sons & Co., and its three partners, under Section 66 (1) of the Income-tax Act, asking us to refer to the High Court of Bombay certain questions of law said to arise out of the orders of the Tribunal made in the Regular Assessment Appeals Nos. 184, 187, 188, and 189 (Bombay) of 1941-42.

2. The only dispute in the appeals was as regards an item of Rs. 7,20,000 in the assessment of the firm, and as it affected the assessment of the partners, the appeals were consolidated and a common order was passed in the firm's appeals in R.A.A. No. 184 (Bombay) of 1941-42. It will therefore be convenient to consolidate all the four applications in one reference, and dispose them of through a common statement of the case.

3. All the facts on which our judgment is based have been stated in detail by us in our order, dated 23rd June, 1942, in R.A.A. No. 184 (Bombay) of 1941-42. They may be summarised as below :—

(*i*) Messrs. Vissonji Sons & Co., took over the managing agency of the Acme Manufacturing Co., Ltd., in 1920. The appellant firm consists of three partners who are also partners in the managing agency firm. These partners also hold major portion of the shares in the Acme Manufacturing Co., Ltd. The company owed the managing agents a large amount of money and a sum of Rs. 7,20,000 was voluntarily given up by them in the scheme of reconstruction of the company.

(*ii*) A comparative study of the balance-sheets of the company from 1921 shows that the company was very much under-capitalised and the capital subscribed was not even enough to meet the cost of the block assets.

(*iii*) In 1924, the advances made by the appellant firm amounted to Rs. 10 lacs, and this amount increased to a sum of over Rs. 15 lacs at the end of 1938.

(*iv*) Further advances were given without any security and in spite of the shaky position of the company which had lost all its paid up capital.

(*v*) The appellants only used to charge interest on the amounts exceeding Rs. 10 lacs.

(*vi*) The appellants actually used to pay interest on moneys borrowed and advance the same to the company without interest up to Rs. 10 lacs and without any security.

(*vii*) No other advance was made by the appellants in the ordinary course of their money-lending business in similar circumstances.

(*viii*) The managing agents owned between themselves and their relations about 96 per cent. of the total capital of the company.

(*ix*) The appellants gave up the amount of Rs. 7,20,000 and the major portion of the corresponding benefit went to the shareholders where the appellants themselves were largely interested.

(*x*) The profit-sharing ratio in the managing agency firm was the same as the profit-sharing ratio as between the partners of the appellant firm.

(*xi*) The new shares issued by the company were taken up by the partners of the managing agency firm in the same proportions as their profit-sharing ratio.

(*xii*) The net effect of foregoing the sum of Rs. 7,20,000 ultimately resulted in an increase of the value of their shares.

(*xiii*) The appellants got exclusive right for the purchase of B class shares of the company which had certain valuable rights attached to them.

4. Relying upon these facts we held that the amount of Rs. 7,20,000 given up by the appellants in the scheme of reconstruction of the company was not money advanced by them in the ordinary course of their money-lending business.

5. Here we would like to deal with certain errors of fact which are alleged to have crept in our appellate judgment (in R.A.A. No. 184-Bombay of 1941-42). They were not at all material in deciding the point before us, and, with the exception of the two detailed below, objections regarding the rest have been withdrawn by the learned Counsel for the applicants before us :—

(a) That Messrs. Mathuradas Vissonji & Co., were not the first managing agents but took over the managing agency from Messrs. J. Gordhandas & Co., in 1920, the company having been floated a few months earlier.

(b) That all the partners of the appellant firm were the partners of the managing agency firm, not from its inception but after July, 1923.

6. The only question of law which arises from our judgment is as follows, and we refer the same to the High Court of Bombay under Section 66 (1) of the Income-tax Act :—

Question referred.—Whether in the circumstances of the case it was rightly held that the sum of Rs. 7,20,000 let off by the appellants in the scheme of reconstruction of the Acme Manufacturing Co., Ltd., was not money advanced in the ordinary course of their money-lending business; and that, therefore, it could not be claimed as bad debt under Section 10 (2) (xi) of the Income-tax Act?"

F. J. Coltman with *Y. B. Rege* and *M. A. Mody*, for the assessees.
M. C. Setalvad with *G. N. Joshi*, for the Commissioner.

JUDGMENT.

BEAUMONT, C. J.—This is a reference made by the Income-tax Tribunal under Section 66 (1) of the Income-tax Act. The question referred to the Court is: "Whether in the circumstances of the case it was rightly held that the sum of Rs. 7,20,000 let off by the appellants in the scheme of reconstruction of the Acme Manufacturing Co., Ltd., was not money advanced in the ordinary course of their money-lending business; and that, therefore, it could not be claimed as bad debt under Section 10 (2) (xi) of the Income-tax Act?" It will be noticed that the question is limited in its character. It is only whether the Tribunal were right in finding that this Rs. 7,20,000 was not advanced in the ordinary course of the appellant's money-lending business. If we hold that the Tribunal were wrong in that finding and that the sum was lent in the ordinary course of business it would follow from the facts found, to which I will refer in a moment, that further questions would arise, whether the cancellation of the debt was in the ordinary course of business and, if so, whether it took place during the year of assessment. However, those questions have not been referred to us. The question referred to us appears on its face to be one of fact; whether the sum advanced was in the ordinary course of business, and the only question of law that arises is whether there was evidence to justify the finding.

The facts are stated in the judgment of the Tribunal and are summarised, and in two respects corrected, in the case submitted to this Court. The assessee firm are Vissonji Sons & Co., who carry on money-lending business, and it would appear that another firm, Mathuradas Vissonji & Co., became managing agents of the Acme Manufacturing Co., Ltd., in 1920, having taken over the agency from another firm called J. Gordhandas & Co., and from July, 1923, the partners in Vissonji Sons & Co., that is, the assessees, and in Mathuradas Vissonji & Co., have been the same persons. In law a firm has no existence independently of its partners, and if there are two firms consisting of exactly the same partners, the real position in law is that

there is only one firm. It may carry on separate businesses, and may carry on those businesses in different names but in fact there is only one firm in law. I think there is a certain amount of confusion, if I may say so, in the case arising from the failure to appreciate that at the material dates, there was in law only one firm. There is a finding of fact that the company owed the managing agents a large amount of money, and that the sum of Rs. 7,20,000 was voluntarily given up by them in the scheme of reconstruction of the Acme Manufacturing Co., Ltd. Well, that seems to be a finding that this loan was really owned by the firm in respect of its managing agency business, and not in respect of its money-lending business, and that is really vital. It is then found that on this loan no interest was charged and that no other advance was made by the assessees in the ordinary course of their money-lending business in similar circumstances. It is then found that the Acme Manufacturing Co., Ltd., being in difficulties, was reconstructed, I gather, in the year of assessment, though that is not found. As part of the scheme of reconstruction the managing agency firm, which at that time was the same in law as the assessees, gave up this debt of Rs. 7,20,000. The partners in the firm were entitled to the great bulk, indeed 96 per cent., of the shares in the company. Whether the partners were entitled to the shares in the same proportion as they were entitled to the shares in the firm seems to me irrelevant. The Tribunal have further found that the result of the cancelling of this debt of Rs. 7,20,000 was to enhance the value of the shares in the company, and therefore, to benefit the owners of the debt in their capacity as shareholders. There cannot, I think, be any question that there was ample evidence to justify these findings. We do not know the circumstances in which the advance of Rs. 7,20,000 was made originally but on the findings of fact, to which I have referred, it seems to me that it was treated as a loan by the managing agents, and in my opinion, there is ample evidence to justify the finding of the Tribunal that this advance was not made in the ordinary course of the assessees' money-lending business. The circumstances, that no interest was charged upon the loan, and that it was given up in order to facilitate carrying out the reconstruction scheme, are entirely against the view that it was an advance made in the ordinary course of money-lending business. To my mind, the only question of law that arises is whether there was any evidence to justify the finding of fact by the Tribunal, and I can only answer that by saying that there was ample evidence.

I think, therefore, we must answer the question raised in the affirmative. The assessees to pay costs.

CHAGLA, J.—I agree. *Reference answered in the affirmative.*

[IN THE LAHORE HIGH COURT.]

COMMISSIONER OF INCOME-TAX, PUNJAB

v.

BHOJRAJ HARICHAND.

DIN MOHAMMAD and MEHR CHAND MAHAJAN, JJ.

October 2, 1945.

INDIAN INCOME-TAX ACT (XI OF 1922), SEC. 10 (2) (xii)—BUSINESS EXPENDITURE—MANUFACTURE OF SALTPETRE—SUM SPENT IN ACQUIRING LEASES OF SALT BEARING LANDS—WHETHER ALLOWABLE DEDUCTION.

The assessee carrying on a business of manufacturing saltpetre acquired year after year leases of lands containing deposits of crude saltpetre. The period of each lease varied in accordance with the saltpetre available from them. The leases had durations of five to ten years and in certain cases lesser or greater. Under the terms of the leases the assessee was entitled to remove two inches of earth containing saltpetre and to take the same to any place he liked :

Held, *that the true nature of the transactions was that of a sale of earth, or of saltpetre or of the recurring yearly saltpetre crop on these lands by the owners of the lands to the assessee, coupled with a licence to the assessee to enter on the lands for the purpose of removing the crude saltpetre, and the expenditure incurred by the assessee for acquiring the so-called leases was not capital expenditure but revenue expenditure and was allowable under Section 10 (2) (xii) of the Indian Income-tax Act.*

Held further, *that the fact that the leases in question were for five to ten years and not short term leases could not make any difference.*

Decision in *Parma Nand Haveli Ram* v. *Commissioner of Income-tax, Lahore [1945] (13 I.T.R. 157 ; A.I.R. 1945 Lah. 137) followed but observations of Munir, J., with regard to long term leases dissented from.*

Cases referred to :—

City of London Corporation *v.* Styles [1887] (2 Tax Cas. 239 ; 4 T.L.R. 51).

Golden Horse Shoe Ltd. *v.* Thurgood ([1934] 1 K.B. 548 ; 150 L.T. 427 ; 103 L.J.K.B. 619 ; 18 Tax Cas. 280).

Parma Nand Haveli Ram *v.* Commissioner of Income-tax, Lahore [1945] (13 I.T.R. 157 ; A.I.R. 1945 Lah. 137).

Case referred by the Commissioner of Income-tax, Delhi, Punjab and North West Frontier Province, Lahore, under Section 66 (1) of the Indian Income-tax Act, for orders of this Court : Civil Reference Case No. 26 of 1943.

STATEMENT OF CASE.

"These are three applications, *viz.*, 66 R. A. Nos. 2, 3 and 4 (Punjab) of 1942-43 by the Commissioner of Income-tax, Punjab, requiring us to refer under Section 66 (1) of the Income-tax Act a question of law which is said to arise out of our orders, dated April 21, 1942, in R. A. A. Nos. 11, 12 and 13 (Punjab) of 1941-42.

2. During the proceedings for the assessment year 1938-39 before the Income-tax Officer the assessee, as usual, claimed as business expenditure under Section 10 (2) (xii) of the Income-tax Act the moneys expended by him in acquiring lease of lands for the purpose of extracting saltpetre therefrom. The following extract from the Income-tax Officer's order explains the nature of the claim:—

'The assessee has so far been erroneously enjoying the benefit of the amount spent by him in acquiring the leases of lands from which crude saltpetre is extracted and brought for refining. These leases of lands are acquired year after year from several persons including Government on contract basis and the period of each lease varies in accordance with the saltpetre available from them. These leases have durations of 5 to 10 years and in certain cases lesser or greater. The assessee has maintained a separate account regarding the leases of lands in which the money invested from time to time and other expenses incurred are credited and debited in accordance with the requirements or durations of the various leases. Out of the net balances in hand proportionate sums of money calculated upon the duration and the amount of the full lease terms are charged to the revenue account for determining the assessable income. The worked-out lease amount for this particular year is Rs. 38,059.'

3. The Income-tax Officer was of the opinion that the facts of the case were on all fours with the facts in *Shankar Shambaji Gangla* v. *Commissioner of Income-tax, Bombay* [1], *Commissioner of Income-tax, United Provinces* v. *Tika Ram & Sons, Ltd.* [2], and *U. Chengalvaroya Mudaliar* v. *Commissioner of Income-tax, Madras* [3]. The only distinction that he could see was that the above-mentioned decisions did not relate particularly to saltpetre manufacturers. Relying upon these authorities, the Income-tax Officer concluded that the expenditure in question was in the nature of capital expenditure and rejected the assessee's claim in his assessment order, dated February 29, 1940. Similar claims in respect of the 1939-40 and 1940-41 assessments were rejected on the same reasoning by relevant assessment orders, dated April 19, 1940, and November 30, 1940, respectively.

(1) (1936) 9 I.T.C. 350. (2) (1937) 5 I.T.R. 544. (3) (1934) 2 I.T.R. 395; 7 I.T.C. 323.

4. The assessee preferred appeals to the Appellate Assistant Commissioner, who in his order, dated February 24, 1941, relating to the 1938-39 assessment, upheld the view taken by the Income-tax Officer and repelled the assessee's contention. The appeals on this issue relating to the two subsequent years' assessments were similarly dismissed by the Appellate Assistant Commissioner's orders dated February 24, 1941, in each case.

5. The assessee preferred appeals to the Tribunal against the three above-mentioned orders. By its orders dated April 21, 1942, in R. A. A. Nos. 11, 12 and 13 (Punjab) of 1941-42 the Tribunal, for the reasons mentioned in the Tribunal's order in R. A. A. No. 63 (Punjab) of 1941-42, held that the expenditure incurred on the acquisition of leases is, in these cases, in the nature of revenue expenditure and therefore allowable as a deduction under Section 10 (2) (xii) of the Income-tax Act. In this view the three appeals were allowed by the Tribunal. The present applications arise out of the above-mentioned orders, dated April 21, 1942, in R. A. A. Nos. 2, 3 and 4 (Punjab) of 1941-42.

6. The original applications were received on June 25, 1942, and heard on August 13, 1942, in which the findings of fact arrived at by the Tribunal were not questioned as being based on no material. The respondent in his reply pointed out that unless the applicant wanted to say that the findings of fact were not supported by any material on record, no question of law could be said to arise out of the orders of the Tribunal. The Departmental Representative thereupon requested permission to put in amended applications. Permission was granted and the amended applications were presented on September 15, 1942, wherein the applicant questions the existence of material on which the findings of fact arrived at by the Tribunal are based. The applicant further states that in arriving at the findings of fact the Bench of the Tribunal committed an error of law inasmuch as it misinterpreted the provisions of Section 10 (2) (xii) of the Income-tax Act in holding the disputed expenditure as revenue expenditure. Lastly, it is stated that the Bench of the Tribunal committed an error of law in drawing inferences from the terms of the leases and other evidences on record.

7. In paragraph 4 of his reply filed under rules 53 and 54 of the Appellate Tribunal Rules, the respondent has correctly set out what took place at the hearing and the material upon which the Tribunal found that the expenditure in dispute was incurred out of the funds set apart by the assessee for the purchase of raw materials. The respondent denies that any question of law arises out of the orders of the Tribunal. The finding that such expenditure amounts to no more

than the purchase of raw materials for the assessee's manufacturing business is an inference drawn from facts.

8. We are of the opinion that the following question of law arises out of our orders, which we refer to the High Court of Judicature at Lahore under Section 66 (1) of the Income-tax Act :—

'Whether in the circumstances found by the Tribunal in which the assessee carries on his business of saltpetre manufacture, the moneys spent in acquiring the leases of lands containing deposits of crude saltpetre have correctly been treated as expenditure in the nature of revenue expenditure allowable as a deduction under Section 10 (2) (xii) of the Income-tax Act ?' "

COPIES OF LEASES.

Translation of the agreement of mortgage executed by Khannu etc., in favour of Seth Harichand son of Seth Bhoj Raj, Proprietor of the lessee's firm.

" We, Khannu son of Quim, Sada son of Muttali, Wali son of Mehra, Sardara son of Qadu, Sahbu and Bahadar sons of Karam, caste Lak, residents of Kot Momin Tehsil Bhalwal—Whereas in the Abadi of Kot Momin compound of the house of Mehar boundaries of which are as under :—

North : Street, South : Abadi Deh, East : Street Jahan Afghani, West : Abadi, there is earth containing saltpetre. The same compound along with the ways thereto along with any other place or places where earth containing saltpetre is found, are leased out for a period of 10 years commencing with 19th February 1935 and ending with 18th February 1945 for the sum of Rs. 130 in favour of Seth Harichand son of Seth Bhoj Raj, caste Mohmta, proprietor of saltpetre factory Phullarwan for the purposes of extracting saltpetre from there. The lease is made through Pt. Harbans Lal to whom possession has been delivered at the spot. The mortgage amount (lease money) will be recovered from the mortgagee in the presence of the Sub-Registrar Bhalwal. During the period of lease the mortgagee shall be entitled to remove earth containing saltpetre and to take the same to any place he likes. We undertake the responsibility on behalf of the co-owners who are absent today and agree that if any of the co-owners will interfere in the work of the lessee we too shall be liable for the damages suffered by the lessee. This agreement of mortgage for a fixed period is therefore executed. Dated 19th February 1935."

Translation of the lease deed executed by Rahman etc., in favour of Seth Harichand son of Seth Bhojraj, Proprietor of the lessee's firm.

" We, Rahman and Karam sons of Ali Raja and Mohamed sons of Mehar Bakhsh, Mandra son of Badar, caste Bhatti, Nur Mohamed son

of Mohamed Din, Dost Mohamed son of Mohamed Sadiq, Abdul Kareem son of Ghulam Mohamed, Alf Din son of Mohamed Din, caste Panjotha, Mian Mohamed son of Ghulam Haidar, caste Panjotha, Salehon and Nur Mohamed sons of Alam, Ata Mohamed son of Rukadin, caste Panjotha, Mussa son of Quaim Isa and Fatta sons of Hussain, Hayat son of Allah Dad, Ghulam Mohamed son of Taja, Murad son of Karam, Gul Mohamed son of Taja, Raja, Murad and Haidar sons of (illegible) caste Hijra, Raja son of Piran, caste Bhatti, their own behalf and on behalf of sons of Karam and sons of Salehon, and Islam son of Khuda Bux residents of Lalilani Tehsil Bhalwal, we agree to lease out all our land under our havelis and demolished houses for the purpose of extracting saltpetre at Rs. 60 per annum in favour of Seth Hari Chand son of Seth Bhojraj, proprietor of saltpetre factory, Phullarwan, for a period of 5 years, *i.e.*, from 19th February 1939 to 18th February 1944, and agree that the said lessee shall be entitled to remove earth for the purpose of using the same for manufacturing saltpetre. He shall not however remove foundations of our demolished houses and will not stand in our way if we wish to erect any room. We shall not interfere in the business of the lessee and if we do that our person and property will be liable to the lessee for all losses. We shall get mutation effected and execute this deed so that it may be used in time of need. Dated 19th February 1939 P.S. The mortgagees will not be entitled to stand in the way of any of the shareholders of the land if any of them wishes to erect any room on this land."

S. M. Sikri and *Jindra Lal*, for the Commissioner.

Kundan Lal Gosain, for the assessee.

JUDGMENT.

MEHR CHAND MAHAJAN, J.—Messrs. Bhojraj Harichand are saltpetre merchants of Phullarwan. The business carried on by them is simple in nature. Crude saltpetre is either bought from the market or extracted from land acquired for the purpose of removing the saltpetre deposits therefrom. The earth containing the saltpetre is scraped and brought to the manufactory where it is boiled in water. The earth is allowed to settle down and the water is separated in boxes where it crystallizes. Prior to the year 1938-39, this firm in assessments of income-tax enjoyed the benefit of the amounts spent in acquiring the leases of lands from which crude saltpetre was extracted and brought for refining, in other words, the rent paid by the assessee in acquiring the leases for extracting crude saltpetre was allowed as business expenditure under Section 10 (2) (xii) of the Income-tax Act. In the year 1938-39, however, the Income-tax Officer concluded that the expenditure

a question was in the nature of capital expenditure and rejected he assessee's claim in his assessment dated February 29, 1940. Similar claims in respect of 1939-40 and 1940-41 assessments were ejected on the same reasoning by relevant assessment orders dated April 19, 1940, and November 30, 1940, respectively. The Appellate Assistant Commissioner upheld the orders of the Income-tax Officer in respect to these assessments. The assessee preferred appeals to the Income-tax Tribunal and the Tribunal was of the opinion that the expenditure incurred on the leases in dispute amounted to no more than the purchase of raw material for the appellant's manufacturing business and as such the expenditure in question was in the nature of revenue expenditure and was, therefore, a legitimate deduction under Section 10 (2), clause (xii), of the Income-tax Act. In the result the appeals were allowed and the assessee's contention was upheld. It was observed by the Tribunal that the facts of each case have to be subjected to the most suitable test that may be applicable to them and that the question of distinguishing capital from revenue expenditure cannot be solved by the application of any hard and fast rule. Reliance was placed in this connection on the observations of Lord Justice Bowen in the *City of London Corporation case*[1] wherein about capital his Lordship said, "You do not use it 'for the purpose of' your concern,...but you use it to acquire the concern" and it was found that in the present case the expenditure was incurred for the purpose of carrying on the existing business of saltpetre manufacture and the manufactory itself was not established as a consequence of the acquisition of the leases in dispute. Towards the concluding portion of the judgment of the Tribunal reference was made to the case of *Golden Horse Shoe Ltd.* v. *Thurgood*[2] and the following observations of the Master of the Rolls in that case were quoted:—

"If the metaphor of working a mine be applied, it might be said that the purchase of the dumps was a capital outlay. If the metaphor of making gas or coke from coal, or of a miller making flour from wheat, be applied, it may be said that it was an outlay to be placed in the profit and loss account. But metaphors do not provide exact definitions and are often misleading. It is safer to give an interpretation to the facts of this case as found in the case stated, and upon the law relevant to them."

In view of these observations his Lordship came to the conclusion that the facts of that case seemed to point to a manufacturing business acquiring raw materials already won and gotten rather than to the analogy of extracting ore from a mine. It was thus observed that in the

(1) (1887) 2 Tax Cas. 239. (2) (1934) 18 Tax Cas. 280, at p. 298.

case before the Tribunal the facts of the case pointed to the obtaining of raw material and not to the extraction of ore from a mine. It further held that the land containing saltpetre deposits could not be described as a wasting asset.

The Commissioner of Income-tax was dissatisfied with the decision of the Tribunal and he made three applications to the Tribunal under Section 66 (1) of the Income-tax Act requiring the Tribunal to state a question of law for the decision of this Court. As a result of these applications the following question of law was referred to this Court under Section 66 (1) of the Income-tax Act :—

"Whether in the circumstances found by the Tribunal in which the assessee carries on his business of saltpetre manufacture, the moneys spent in acquiring the leases of lands containing deposits of crude saltpetre have correctly been treated as expenditure in the nature of revenue expenditure allowable as a deduction under Section 10 (2) (xii) of the Income-tax Act ?"

In the case of *Messrs. Parma Nand Haveli Ram* v. *Commissioner of Income-tax*[1], the following question of law was referred to this Court and was decided by a Full Bench :—

"Whether the money called lease money paid to the owners of the lands from which saltpetre was extracted as a consideration for the licence granted by the said owners for the use of their lands for the purpose of such extraction during the year was a capital expenditure and could not be deducted as a legitimate expense incidental to the business ?"

The Full Bench gave the answer that the money expended on the leases should not be regarded as a capital expenditure in the circumstances of the case. The principles on which the Full Bench arrived at its decision are enunciated at page 144 of the report in the following terms :—

"The present case is not one where the assessee's business consists of working a particular bed since it has been found by the Commissioner that for the purposes of his business the assessee acquires a large number of leases which are exhausted in the course of a year or so. In my opinion, therefore, this is precisely the case which was contemplated by Channell, J., when he said that if the business of the assessee had been merely a manufacturing business or if in the course of carrying on his business the assessee had to acquire and develop similar properties the decision would have been otherwise. The case is one of exceptional difficulty as no parallel case has been cited before us which could have assisted us in the decision of the precise point

(1) (1945) A.I.R. 1945 Lah. 137 ; 13 I.T.R. 157, at p. 169.

involved in the case, which is that though the predominant character of the assessee's business is that of a manufacturing business, the assessee does not purchase his raw material in the ordinary way from the market but procures it by a process of collection and manufacture. The raw material for the assessee's business of manufacturing crude saltpetre is the salt bearing earth which is not a marketable commodity and according to the customary usage can only be acquired by obtaining short term leases from the proprietors of the villages where such earth is found. The essential point is that the semi-manufactured produce, *i.e.*, crude saltpetre, is not sold by the assessee in the market and is acquired by him for the sole purpose of converting it into the finished product, *i.e.*, potassium nitrate and sodium chloride. The assessee extracts by the process of evaporation as much crude saltpetre as he can economically obtain during the short period of the lease and sends the entire stuff to the refinery and does not make any profit by selling the crude saltpetre. According to the ordinary method of calculating the profits or gains of a business, therefore, the assessee must deduct from his sales the money expended in acquiring salt bearing earth under the short term leases, because such expenditure must enter into the costs of production of the finished product. In the course of arguments both parties cited a large number of English cases which define the considerations which affect the determination of the question whether a certain expenditure is capital or revenue. Applying those considerations we find that the money expended by the assessee in acquiring the sites for the purpose of extracting crude saltpetre is not expended in acquiring the assessee's business but for the purpose of running it."

The reference before us is covered by the principles enunciated by the Full Bench and must be answered on similar lines and the decision of the Tribunal must be affirmed.

Mr. Sikri, learned counsel for the Commissioner of Income-tax, attempted to distinguish the Full Bench case from the case before us on the ground that the leases in the Full Bench case were short term leases while in the present case the leases ranged from five to ten years. He placed reliance on the following observations contained in the leading judgment of the Full Bench delivered by Munir, J.:—

"The assessee's business is an existing business in the course of which he has got to acquire sites for the purpose of extracting raw material and it cannot, therefore, be said that each lease into which the assessee enters constitutes an independent venture the profits of which must be worked out separately. It is thus impossible to hold that the expenditure in question was incurred by the assessee for the

purpose of acquiring a business and not for the purpose of running a business. The periods of the leases as found by the Commissioner range from one year to two years and for that reason these leases cannot be said to bring into existence an asset or an advantage for the enduring benefit of the trade. The expenditure is a running expenditure which is a very important and in this case the determining consideration to answer the question whether the expenditure is capital or revenue. Since the expenditure is not capital according to the three broad tests just mentioned and because it is unquestionably a revenue expenditure according to ordinary principles of trade, it should, I think, be held to be a revenue expenditure. The result may perhaps be different where the land worked is the property of the assessee, or is acquired by him on a long term lease, because in such a case the rights in the land would be a fixed capital asset. But where, as in this case, the assessee must from year to year spend a large amount to acquire the right to collect *kallar* for a year or so, the expenditure does not become capital merely by reason of the fact that what is acquired is not *kallar* but the right to collect *kallar*, and such expenditure is as much a revenue expenditure as the expenditure in purchasing raw material by a manufacturer or stock-in-trade by a trader."

The observations contained in the concluding portion of the passage cited above are clearly obiter in their nature and do not furnish any authority or guide for the decision of the point raised by Mr. Sikri. On the broad principles enunciated in the Full Bench judgment that the expenditure is a running expenditure and is a revenue expenditure according to ordinary principles of trade, the question of the duration of the leases could not lead to a different conclusion. With great respect to my learned brother Munir, J., I cannot assent to the obiter observations that his Lordship made in the concluding portion of the passage cited above. If according to ordinary principles of the trade of the assessee the crude saltpetre obtained from the leased lands is merely raw material, then whether the raw material is obtained for a number of years or only for a year or so cannot affect the decision of the case and alter the nature of the revenue expenditure into capital expenditure. In view, therefore, of the broad principles enunciated in the Full Bench decision I am of the opinion that the reference before us is concluded by that decision with which we are bound.

Mr. Sikri contended that the real matter for decision in all such cases is whether the trader or the manufacturer has purchased raw material or acquired land under a lease for the manufacture of raw

material itself; in other words if he acquires lease of land, *i.e.*, something from which raw material can be got, that transaction cannot amount to the purchase of raw material and, therefore, the leasehold rights must be held to be capital expenditure. That contention of Mr. Sikri, if entertained, would compel us to go behind the Full Bench decision which we are not competent to do. On that argument the question of the term of the lease or its duration becomes wholly irrelevant. We cannot, therefore, entertain it. That being so, the answer to this reference must be in the affirmative and the Commissioner's contention must be repelled.

It must further be stated that in the present case the Tribunal observed that on the facts of the case it was clear that the assessee by means of these so-called leases was obtaining raw materials and the object was not the extraction of ore from a mine. In substance it came to the conclusion that the transactions of leases amounted to no more than the purchase of raw materials for the assessee's manufacturing business. Some of the leases by means of which saltpetre was acquired by the assessee have been read to us and are printed in the paper-book. A perusal of these leases clearly shows that the transactions in fact were for the purchase of the earth for using it for manufacturing saltpetre. It is really incorrect to describe these transactions as leases. The true nature of these transactions is that of the sale of earth, or of the saltpetre or of the recurring yearly saltpetre crop on these lands by the owners of the lands to the assessee and a licence has been given to the purchaser to enter on the lands for the purpose of removing the crude saltpetre. It may be mentioned that it is within two inches of the surface of the earth that the saltpetre comes out twice a year and it is that portion of the earth that is sold to the manufacturer of saltpetre and a licence is granted to him by the owner of the soil. As the crop is a recurring deposit, similarly the lease money in most cases is an annual payment. It is a well-known canon of the construction of documents that intention generally prevails over the words used, and that such a construction should be placed on the words in a deed as is most agreeable to the intention of the grantor. If there are grounds appearing from the face of the instrument affording proof of the real intention of the parties, then that intention would prevail against the obvious and ordinary meaning of the words used. If the parties have themselves furnished a key to the meaning of the words used, it is not material by what expression they convey their intention. Reference in this connection may be made to Odgers on The Construction of Deeds and Statutes, 1939 edition, page 24. If these so-called leases are construed in the light of the above rules of

construction, then I have no doubt in my mind that these various documents are misdescribed as leases. They are really contracts for the sale of the crude saltpetre deposits that emerge on the soil of the grantor biannually and a licence to the purchaser to enter on the soil to collect these deposits. In the case that came before the Full Bench these leases were appropriately described as licences. The purchaser acquires no rights in the land itself. He can only remove this crude saltpetre earth and has no other rights so far as the ownership of the land is concerned. On this construction of these deeds, there can be no question but that the expenditure in question is an allowable deduction under the provisions of Section 10 (2) (xii) of the Indian Income-tax Act and was rightly so allowed by the Tribunal.

For the reasons given above my answer to the reference is in the affirmative.

Perhaps, it will not be out of place to mention that in Civil Reference No. 25 of 1943*, the question referred to this Court was in identical terms as in this case and in the statement of that case it was stated that leases were for duration of five to ten years and in certain cases lesser or greater. In that case the learned counsel for the Commissioner of Income-tax conceded that the Full Bench decision in *Parma Nand Haveli Ram's case*[1] concluded the point, and we answered the reference in the affirmative accordingly.

DIN MOHAMMAD, J.—I agree that the question propounded in this case be answered in the affirmative.

Reference answered in the affirmative.

[IN THE CALCUTTA HIGH COURT.]

COMMISSIONER OF INCOME-TAX, BENGAL

v.

KHAN BAHADUR WALIUR RAHMAN.

GENTLE and ORMOND, JJ. January 22, 1946.

INDIAN INCOME-TAX ACT (XI OF 1922), SECS. 16 (3) (a) (i), 66—PARTNERSHIP—HUSBAND AND WIFE—MANUFACTURE AND SALE OF TEA—WHETHER PARTNERSHIP EXISTS—QUESTION OF FACT—APPLICABILITY OF RULE 24, INCOME-TAX RULES.

Rule 24 of the Indian Income-tax Rules is applicable only in respect of a seller who manufactures tea which he has himself grown and which he himself sells.

* Since reported as *Nand Lal Bhoj Raj, In re* [1946] 14 I.T.R. 181.

(1) [1945] 13 I.T.R. 157.

The assessee and his wife were each possessed of separate properties. The wife's property was not in any way derived from her husband. They grew tea upon lands belonging to each of them, purchased a tea factory and made other arrangements to make and sell tea, each finding a sum for those purposes. The profits derived from the sale of tea were equally divided between them. With regard to the management of the wife's interest the assessee held, together with eight other persons, a power-of-attorney from the wife. The undertaking with regard to the manufacture and sale of tea was known as Rheabari Tea Estate. The Income-tax Officer treated the undertaking as a partnership consisting of the assessee and his wife and included in the assessee's income his wife's income under the provisions of Section 16 (3) (a) (i) of the Income-tax Act. The Income-tax Officer also applied the provisions of rule 24 of the Income-tax Rules. On appeal the Income-tax Appellate Tribunal held that there was no partnership between the assessee and his wife with respect to the tea estate :

Held, (*i*) *that there was evidence on which the Tribunal could come to its finding that there was no partnership between the assessee and his wife* ;

(*ii*) *that rule 24 of the Income-tax Rules was inapplicable inasmuch as the tea which the alleged partnership manufactured and sold was not tea which was grown by that partnership.*

In the matter of an application under Section 66 (2) of the Indian Income-tax Act (XI of 1922, as amended by Act VII of 1939) and in the matter of Reference 66 R. A. No. 4—Bengal of 1942-43 in the Appellate Tribunal (Income-tax), Calcutta Bench, arising out of Appeal R.A.A. No. 81 (Bengal of 1941-42): Income-tax Reference No. 5 of 1943.

S. K. Gupta with *J. C. Pal*, for the Commissioner.

R. B. Pal with *A. C. Sen*, for the assessee.

JUDGMENT.

GENTLE, J.—This is an application by the Commissioner of Income-tax, Bengal, for an order calling upon the Income-tax Appellate Tribunal to state a case on questions of law with respect to its order relating to an assessment for the year 1938-39 made upon Khan Bahadur Waliur Rahman of Jalpaiguri. On the 17th January, 1944, this Court issued a rule nisi calling upon the Tribunal to show cause why a case should not be stated and this is the hearing of the rule which was served not only on the Tribunal but also on the assessee. Since the issue of this application the assessee had died and his sons and daughters have been brought on the record as his legal representatives. No point arises out of this.

It is convenient first to state the relevant facts. The assessee and his wife, Begum Manija Khatun, are each possessed of separate properties, the wife's property was in no way derived from her husband and she obtained it from other sources. Each of them is the proprietor of lands, portions of which are adjacent to each other. Having obtained the necessary permits from the Government, the assessee and his wife commenced to grow tea upon lands belonging to each of them, adjacent to one another's property. In order to put the crop into a marketable state, a tea factory was purchased and other arrangements were made to make and sell tea, the husband and the wife each finding a sum for those purposes. After manufacture the tea is sold and the proceeds, or more correctly, the profits of the proceeds, are equally divided between the assessee and his wife. With regard to the management of the wife's interest in the growing of the crop, its manufacture and sale, the husband holds, together with eight other persons, a power-of-attorney from the wife enabling him and the others to deal with matters which require attention with respect to those arrangements. It is no part of the applicant's case that the separate pieces of adjacent lands belonging to the husband and the wife ever ceased to be other than their respective separate properties.

The undertaking, as I will call it, with regard to the manufacture and sale of tea, is known as the Rheabari Tea Estate and, so far as it is material, up to the year of assessment 1938-39, the profits from that undertaking were assessed as upon an association of individuals. In respect of the year under consideration the Income-tax Officer considered that the husband and the wife were partners together in the Rheabari Tea Estate. Consequently, he applied the provisions of Section 16 (3) (a) (i) of the Income-tax Act which reads as follows:—

"In computing the total income of any individual for the purpose of assessment, there shall be included so much of the income of a wife as arises directly or indirectly from the membership of the wife in a firm of which her husband is a partner."

The Rheabari Tea Estate was treated as a partnership and the result of the new method of assessment was to include in the husband's income-tax assessment that part of the profits from the Rheabari Tea Estate as were considered to belong to the wife, and for the purpose of assessment that income was treated as part of the husband's income.

In making his assessment the Income-tax Officer applied the provisions of rule 24 of the Indian Income-tax Rules, as then in force which are as follows:—

"Income derived from the sale of tea grown and manufactured by the seller in British India shall be computed as if it were income

derived from business, and 40 per cent. of such income shall be deemed to be income, profits and gains liable to tax."

It will be noticed that this rule is applicable only in respect of a seller who manufactures tea which he has himself grown and which he himself sells. It is no part of the case of the Commissioner that the two pieces of land belonging to the husband and the wife are parts of the assets of a partnership or that the crops grown on the lands are such assets but the crops become part of the assets when plucked or when delivered into the tea factory for manufacture. That being the position, it does not seem, whatever other considerations there may be, that rule 24 should be applicable inasmuch as the tea, which the alleged partnership manufactures and sells, is not tea which is grown by that partnership. The substance of the assessment made by the Income-tax Officer should be, since rule 24 has been applied, that the partnership grew the crop from which tea was manufactured.

The assessee appealed against the application of Section 16 (3) (a) (i) and the inclusion in his assessment of his wife's share from the profits of the Tea Estate to the Appellate Assistant Commissioner who dismissed that appeal. He further appealed to the Income-tax Appellate Tribunal. That body allowed the appeal holding that there was no partnership between the husband and the wife with respect to the tea estate.

Being dissatisfied with its decision the Commissioner applied to the Tribunal to state a case upon questions which he formulated. The Tribunal by its order held that no point of law arose for the opinion of this Court and refused to state a case. The present application is made under the provisions of Section 66 of the Act to require the Tribunal to state a case.

There were two questions which the Commissioner sought to raise and in respect of which he applied to the Tribunal to state a case. They are as follows :—

"(1) Whether there were any materials on which the Tribunal could come to the finding recorded in paragraphs 3, 4 and 5 of their order, and

(2) Whether on the admitted facts and circumstances of the case the Tribunal directed themselves correctly in holding that there was in law no partnership between the assessee and his wife and Section 16 (3) (a) (i) of the Income-tax Act did not apply."

Dr. Gupta, learned counsel for the Commissioner, at the commencement of his argument, formulated two questions which, if I may say so, more succinctly and correctly would set out the contention

which he sought to establish in his argument, but I do not think, save for the method of expression, there was any alteration in the substance of the questions which the Tribunal was asked to state and which it refused to do.

Before I deal with other matters reference to some of the provisions of Section 6 of the Partnership Act is convenient. They are as follows :—

"In determining whether a group of persons is or is not a firm, or whether a person is or is not a partner in a firm, regard shall be had to the real relation between the parties, as shown by all relevant facts taken together.

Explanation 1.—The sharing of profits or of gross returns arising from property by persons holding a joint or common interest in that property does not of itself make such persons partners."

I refer to the above provision because it is not, as the enactment declares, a necessary corollary that because two persons share the profits arising out of the same property these persons are in partnership together with respect to it.

I have set out the facts and circumstances which have appeared in this reference. From those facts it was open to the Tribunal to decide, aye or nay, whether the husband and the wife were partners in the Rheabari Tea Estate. The Tribunal has decided that there was no partnership. Whether that decision is correct or whether it is incorrect, to my mind, is not a matter with which we are concerned. It was open to the Tribunal to express a finding one way or the other and it has done so. Question (1) is whether there were any "materials" which I can read only as "evidence," on which the Tribunal could come to its finding. In my opinion, there was evidence, and that being so, it is not for this Court to correct any error which there may be, but which I do not say there is, in the conclusion to which the Tribunal arrived. In the way in which the question appears to be framed and using the word "evidence" instead of materials, it would seem that what was sought to be raised is whether there was any evidence on which the Tribunal could find that there was no partnership. However, that is a matter which needs no further reference.

Now as to the second question. It relates to admitted facts and circumstances. The question suggests that upon those admitted facts the Tribunal should have come to the conclusion that there was a partnership. It is conceded that the words "admitted facts" include statements which are alleged to be contained in a written document dated the 26th February, 1938, in which the assessee set out certain matters which he sent to the Department. What the document

contains I do not know; it was not placed before the Tribunal, from which one can only infer that reference to it was not made at the hearing before that body. There is no express reference to it in the order of the Appellate Assistant Commissioner. Dr. Gupta referred us to a passage in the Appellate Assistant Commissioner's order which, he says, came from that statement, but there is nothing in the order itself which in any way suggests that any part of it, whatever it contained, is cited by the Appellate Assistant Commissioner; with respect to the second question the so-called admitted facts, alleged to be contained in the assessee's document, were not before the Tribunal inasmuch as the document in which those facts are alleged to be contained was never placed before them.

In my opinion this rule nisi should be discharged. The assessee is entitled to his costs assessed at 12 gold mohurs.

ORMOND, J.— I agree. *Rule nisi discharged.*

[IN THE PATNA HIGH COURT.]

THE PROVINCE OF BIHAR

v.

MAHANTH HARIBHAJAN DAS OF ANDHARI.

FAZL ALI, C. J., MANOHAR LALL and SINHA, JJ.

January 9, 1946.

BIHAR AGRICULTURAL INCOME-TAX ACT (VII OF 1938), SEC. 8—TRUST FOR PUBLIC PURPOSES OF A CHARITABLE AND RELIGIOUS NATURE—WHOLE INCOME—WHETHER EXEMPT—INCOME SHOULD BE SPENT OR "FINALLY SET APART."

The assessee was the mahant of an asthal which had landed properties yielding agricultural income. He was a trustee and the trust under which he held was a trust created before the commencement of the Bihar Agricultural Income-tax Act for public purposes of a charitable and religious nature. He was assessed to agricultural income-tax on a certain sum after allowing a deduction of a sum found to have been spent by him on charitable and religious objects. The assessee contended that as he was holding the properties for public purposes of a charitable and religious nature, the whole of his agricultural income was free from taxation under Section 8 of the Act:

Held, *that the assessee was not exempt from payment of agricultural income-tax under Section 8 of the Act beyond what he had actually spent on religious and charitable objects consistent with the purpose of the trust.*

In order to claim exemption under the Act, the assessee must in each year show that he had finally set apart a sum for charitable and religious purposes.

All India Spinners' Association v. *Commissioner of Income-tax, Bombay* [*1944*] (*12 I. T. R. 482*) distinguished.

Statement of Case under Section 25 (2) of the Bihar Agricultural Income-tax Act (VII of 1938) by the Board of Agricultural Income-tax, Bihar, dated the 28th August 1941, regarding assessment of agricultural income-tax on Mahanth Haribhajan of Andhari: Miscellaneous Judicial Case No. 83 of 1941.

FURTHER STATEMENT OF CASE.

"Further statement of the case by the Board of Agricultural Income-tax, Bihar, under the provisions of Section 25, sub-section (5), Bihar Agricultural Income-tax Act, in compliance with the remand order of the High Court, dated 1-4-1942, in Miscellaneous Judicial Case No. 83 of 1941.*

This reference arises out of two assessment orders, dated 26-5-40, passed by the Agricultural Income-tax Officer, Darbhanga, Babu R.P. Gupta, under the Bihar Agricultural Income-tax Act against Mahanth Haribhajan Das of Andhari in the district of Darbhanga assessing the latter to agricultural income-tax for the years 1345 and 1346 Fasli (*i.e.*, 1938-39 and 1939-40 A.D.). The assessee has been assessed to agricultural income-tax on Rs. 6,229 for the year 1345 Fasli and on Rs. 6,106-8-0 for 1346 Fasli as calculated in the statement A enclosed. From this statement it will appear that an allowance has been made for Rs. 3,500 on account of expenditure on charities and religious objects in the year 1345 Fasli. Similarly an allowance of Rs. 3,248 has been made for 1346 Fasli in calculating the assessable income of Rs. 6,106-8-0 for that year. These allowances are said to have been made in view of the provisions of Section 8 of the Act exempting from assessment any income applied, or finally set apart for application, to any public purpose of a charitable or religious nature. The assessee is the present mahanth of an asthal which has some landed properties yielding agricultural income. The corpus of the properties seems to have been originally granted in 1171 Fasli by virtue of two deeds by the then Maharaja of Darbhanga to one Mahanth Gosain Naru Ram as Brahmottar and Shibottar grant in two blocks of land stipulating that the properties were to be held for the satisfaction of Lord Vishnu (a Hindu deity) and Mahanth Gosain Naru Ram was to hold them on behalf of the deity and for the satisfaction of the deity. It is said that some

* Since reported as *Province of Bihar* v. *Mahant Haribhajan Das of Andhari* [1942] 10 I. T. R. 399.

of the succeeding mahanths have purchased about 300 bighas landed properties yielding agricultural income out of the income derived from the land attached to the asthal and the income from the purchased villages is also spent for public, religious and charitable purposes by the assessee who spends the income derived from the entire properties in any way he likes subject to the main purpose in view, *i.e.*, relating to public, religious and charitable objects. It is also said that the office of the mahanth of the asthal descends by nomination on the death of the previous holder of the office and that the mahanth has to remain a celibate throughout his life. These facts are undisputed and I agree with the finding of the Agricultural Income-tax Officer that the assessee is a trustee and the trust under which he holds is a trust created long before the Bihar Agricultural Income-tax Act came into force for public purposes of a charitable and religious nature.

From the assessment orders (Exhibits A and B) it also appears that the agricultural income of the assessee consists of :—

(1) Collection of rents from tenants, (2) income from orchards of mango and plantain trees, and (3) produce of 400 bighas of lands in khas cultivation. None of these items of income have been challenged by the assessee at any previous stage. Deductions have also been allowed on account of collection charges and cost of cultivation under Sections 6 and 7 of the Act. The assessee has urged that the Agricultural Income-tax Officer has over-estimated the value of the gross produce of the khas cultivation land and has under-estimated the cost of cultivation. The Agricultural Income-tax Officer has given good reasons for calculating the annual value of the produce of 400 bighas of khas cultivation land at Rs. 10,800 and the Board agrees that the valuation is fair and moderate. The figures for the cost of cultivation for 1345 Fasli and 1346 Fasli have been accepted by the Agricultural Income-tax Officer as given in the returns filed by the assessee. Therefore, the contention of the assessee that it has been under-estimated is frivolous.

A further report of the Agricultural Income-tax Officer, Darbhanga, has been obtained. A copy of the report is enclosed.

A history of the case has already been furnished in the statement dated the 28th August 1941. The assessee filed two appeals under Section 22 (1) of the Act against the orders of the Agricultural Income-tax Officer before the Assistant Commissioner of Agricultural Income-tax. The appeals were dismissed under Section 22 (5). He moved the Commissioner of Agricultural Income-tax, Tirhut, for revision of the orders of the Assistant Commissioner under Section 24. Both the revision petitions were rejected. The assessee then filed two petitions, both under Sections 24 and 25 of the Act before the Bihar

Board of Agricultural Income-tax for revision of the orders of the Commissioner of Agricultural Income-tax, Tirhut, with an alternative prayer for a reference to the High Court on the following points of law :—

(1) Whether he is exempted from payment of the agricultural income-tax under Section 8 of the Act, and

(2) Whether if he is not altogether exempted, the assessment for the year 1345 Fasli which was made under Section 26 of the Act, was valid.

As Section 24 of the Act did not provide for a second revision the petitions for revision were rejected but in the opinion of the Board it appeared that a question of law was involved in point No. (1) and, therefore, a reference was necessary. In his assessment orders (Exhibits A and B) the Agricultural Income-tax Officer has allowed a deduction for Rs. 3,500 for the year 1345 Fasli and Rs. 3,248 for 1346 Fasli on account of expenses on charities and religious objects. The figure for 1346 Fasli is based on the account book filed by the assessee and the figure for 1345 Fasli is an estimated figure as the assessee did not file any account book for the year for expenses on these accounts. There does not seem to be any reason to doubt these sums. The assessable income of Rs. 6,229 for 1345 Fasli and of Rs. 6,106-8-0 for 1346 Fasli has been found by the Agricultural Income-tax Officer after deducting the expenses on charities and religious objects mentioned above, holding that under Section 8 of the Act the entire agricultural income of the assessee is not exempted from the payment of agricultural income-tax but only a part of the income which is applied, or finally set apart for application, to any public purpose of a charitable or religious nature. In the opinion of the Board it seems that the view of the law taken by the Agricultural Income-tax Officer is correct that the assessee should not be allowed exemption from the payment of the agricultural income-tax altogether under Section 8 of the Act but only for the amount spent on religious and charitable objects consistent with the purposes of the trust.

With regard to point No. (2) the Board has already expressed its opinion in its order, dated 29-7-41, that no question of law is involved and has, therefore, made no reference on the point."

Advocate-General, for the Province of Bihar.

N. K. Prasad No. II, for the assessee.

JUDGMENT.

MANOHAR LALL, J.—This is a reference under Section 25 (2) of the Bihar Agricultural Income-tax Act (VII of 1938) by the Board of Agricultural Income-tax, Bihar, for our opinion upon the question

whether the assessee is exempt from payment of agricultural income-tax under Section 8 of the Act.

The matter came before this Court in 1942 when this Court was unable to express any opinion on this question because the case stated did not contain sufficient materials. The case was, therefore, sent back to the Board of Agricultural Income-tax, Bihar, for a further statement.* That statement has now been received.

The facts are not in dispute. The assessee is the present mahant of an asthal which has landed properties yielding agricultural income. The assessee has been found to be a trustee, and the trust under which he holds is a trust created long before the Act came into force and is for public purposes of a charitable and religious nature.

For the year 1345 Fasli the assessee has been assessed to agricultural income-tax on Rs. 6,229 after allowing for a deduction of Rs. 3,500 found to have been spent by him on charitable and religious objects. For the year 1346 Fasli the assessee has been assessed on a sum of Rs. 6,106-8-0 after making a deduction for Rs. 3,248 found to have been spent by the assessee on charitable and religious objects.

The assessee's contention is that, as it has been found that he is holding the properties for public purposes of a charitable and religious nature, the whole of his agricultural income is free from taxation and not merely the sum found by the Agricultural Income-tax authorities to have been actually spent for religious and charitable purposes in the two previous years.

In my opinion this contention is not sound. The provisions of Section 8 (1) of the Act are absolutely clear. It is enacted that where the assessee is a trustee and the trust under which he holds is a trust created before the commencement of this Act, for public purposes of a charitable or religious nature, any income applied, or finally set apart for application, to any public purpose of a charitable or religious nature in accordance with the terms of the trust subject to which he holds the property from which such agricultural income is derived, shall not be included in the total agricultural income of such assessee. It has been found that the assessee has actually applied certain sums towards religious and charitable objects in the years of assessment. That sum has accordingly been deducted from the total agricultural income. The assessee can only claim a further exemption if he could show that any other sum has been finally set apart for application to public purposes of a charitable or religious nature. There is no such finding in the statement of the case nor in any of the orders of the subordinate officers because this was not the case put forward by the assessee. His case on the other hand was—and the same contention was advanced here by Mr. Nawal Kishore Prasad No. II—that

*See *Province of Bihar* v. *Mahant Haribhajan Das of Andhari* [1942] 10 I.T.R. 399—Ed.

the whole of the income from agriculture has been finally set apart by the donor for religious and charitable purposes. But in order to claim exemption under the Act, the assessee must in each year show that he had finally set apart a sum for charitable and religious purposes. The words used in the Act are "finally set apart." Take a case of common occurrence. The assessee is in possession of lands yielding Rs. 15,000 per annum as agricultural income which under the terms of the trust he can and must use for religious and charitable purposes. But he may actually use only Rs. 10,000 for religious and charitable purposes, and save the balance for investment in Government securities or in purchasing some land. Can it be said that the sum of Rs. 5,000 has been finally set apart in that year for religious and charitable purposes? In my opinion the question admits only one answer.

Mr. Nawal Kishore Prasad No. II drew our attention to the case of the Judicial Committee in *All India Spinners' Association case* [1], but that was a case decided upon the terms of Section 4 of the Income-tax Act where the relevant provision is that a deduction shall be made if "any income derived from property held in trust or other legal obligation wholly for religious or charitable purposes, and in the case of property so held in part only for such purposes, the income applied, or finally set apart for application thereto." It will be noticed that the words in the Agricultural Income-tax Act are different and impose a limitation, which under the Income-tax Act is prescribed only in case of properties held in part only for religious or charitable purposes, to income derived from property held wholly for religious or charitable purposes. That case, therefore, is of no assistance to the assessee.

In my opinion the answer to the question is that the assessee in the present case is not exempt from payment of agricultural income-tax under Section 8 of the Act beyond what he has actually spent on religious and charitable objects consistent with the purpose of the trust.

It was suggested that we should call for a finding as to whether the assessee has or has not set apart any sum in these two years for religious and charitable objects, but we are unable to agree to this suggestion as the assessee has never sought to establish that he had actually set apart in the two years of assessment any sum for religious and charitable objects. If he had raised any such question and furnished materials for its decision, this question would no doubt have been decided properly.

The assessee must pay the costs of this reference; hearing fee Rs. 100.

FAZL ALI, C. J.—I agree.

SINHA, J.—I agree. *Reference answered accordingly.*

(1) [1944] 12 I.T.R. 482.

[IN THE BOMBAY HIGH COURT.]

D. M. VAKIL *v.* COMMISSIONER OF INCOME-TAX.

KANIA, AG. C. J., and CHAGLA, J. September 17, 1945.

INDIAN INCOME-TAX ACT (XI OF 1922), SEC. 9—INCOME FROM PROPERTY—ANNUAL VALUE—BASIS OF ASSESSMENT—TRUST—BENEFICIARIES ALONE ALLOWED TO OCCUPY TRUST PROPERTY UNDER WILL—WHETHER TRUSTEES LIABLE TO BE ASSESSED ON ANNUAL VALUE.

Under Section 9 of the Indian Income-tax Act, 1922, the tax is to be payable by an assessee in respect of the bona-fide *annual value of the property irrespective of the question whether he receives that value or not. The income from property is an artificially defined income and the liability arises from the fact that the assessee is the owner of the property. The liability does not depend on the power of the owner to let the property, as it also does not depend on the capacity of the owner to receive the* bona-fide *annual value.*

A lady appointed her husband, son and daughters as trustees under her last will and testament. The will provided that during the lifetime of the husband of the testatrix, he, his son and one daughter, and such of the children and grandchildren of the testatrix as might be invited had the right to occupy a bungalow free of rent. The trustees contended that they could not be said to have realised any income whatsoever from the trust property which could be computed under Section 9 and they were therefore not liable to pay any income-tax in respect of that property :

Held, *that the annual value of the property should be included in the assessment of the trustees under Section 9.*

Tennant v. *Smith [1892] A.C. 150,* and *Bejoy Singh Dudhuria* v. *Commissioner of Income-tax [1933] (I.L.R. 60 I.A. 196; 1 I.T.R. 135),* distinguished. *Official Assignee, In re [1937] (5 I.T.R. 233),* relied on.

Cases referred to :—

Bejoy Singh Dudhuria *v.* Commissioner of Income-tax [1933] (1 I.T.R. 135 ; 60 I.A. 196 ; 60 Cal. 1029 ; 143 I.C. 145 ; A.I.R. 1933 P.C. 145 ; 6 I.T.C. 449).

Commissioners of Inland Revenue *v.* Fleming [1928] (14 Tax Cas. 78 ; [1928] Sess. Cas. 759 ; 1928 Sc. L.T. 530).

Currimbhoy Ebrahim Baronetcy Trust *v.* Commissioner of Income-tax [1935] (3 I.T.R. 395 ; 9 I.T.C. 121 ; 40 C.W.N. 199 : 60 I.A. 209).

Official Assignee for Bengal, In the matter of [1937] (5 I.T.R. 233 ; 10 I.T.C. 225 ; I.L.R. 1937, 2 Cal. 192).

Tennant *v.* Smith ([1892] A.C. 150 ; 61 L.J.P.C. 11 ; 66 L.T. 327 ; 3 Tax Cas. 158).

Reference under Section 66 (1) of the Indian Income-tax Act (XI of 1922) by the Income-tax Appellate Tribunal: Income-tax Reference No. 1 of 1945.

STATEMENT OF CASE.

"This is an application under Section 66 (1) of the Income-tax Act to refer to the High Court a question of law arising out of the order of the Tribunal in R. A. A. No. 229 (Bombay) of 1943-44.

2. The late Bai Bhicaiji Dhunjibhoy appointed her husband and her son and three daughters as the trustees under her last will and testament, dated 28th January 1937. It was provided in clause 5 of the said will that during the lifetime of the husband of the testatrix, he, his son Motabhoy and daughter Motibai shall have the right to use and occupy free of rent such portion of the Warden Road property as was at the time of the making of the will occupied by the testatrix and the other members of the family. Besides these persons, such of the children and grandchildren of the testatrix as might be invited were also to have the right to reside in the bungalow but none others.

3. It was urged by the trustees, who were assessed as an association of persons for the assessment year 1942-43, that, in view of the aforementioned provision in the will, the trustees cannot be said to have realised any income whatever from the property in question which could be computed under Section 9 of the Income-tax Act. The claim was rejected by the Income-tax Officer and the income from the said house property was computed on the *bona fide* annual value basis under Section 9 and included in the assessment.

4. On appeal the Appellate Assistant Commissioner held that no income was actually received from the bungalow which was liable to tax under Section 9 and consequently directed the exclusion of the aforementioned item from the calculation of the assessee's property income.

5. The Income-tax Officer appealed to the Tribunal against the Appellate Assistant Commissioner's order and the Tribunal held upon the facts stated above that the mere circumstance that in pursuance of a certain arrangement no rent is to be charged from the occupants of the property does not render the property or the income thereof exempt from assessment under Section 9 of the Act. This conclusion was reached on a scrutiny of the language of Section 9 in relation to the scheme of taxation appearing from the combined operation of Sections 2 (15), 3 and 4 of the Act. In this view, the Tribunal reversed the finding of the Appellate Assistant Commissioner and restored the order of the Income-tax Officer in that behalf.

6. The assessee has applied for stating the case to the High Court and the Commissioner agrees that the finding of the Tribunal gives rise to a question of law. We are of the view that a question of law arises out of the order of the Tribunal and accordingly refer to the High Court of Judicature at Bombay the following question under Section 66 (1) of the Income-tax Act:—

'Whether upon the facts found by the Tribunal, the annual value of the property on Warden Road, Bombay, has been rightly included in the assessment under Section 9 of the Income-tax Act?'"

Y. P. Pandit, for the assessees.

M. C. Setalvad, for the Commissioner.

JUDGMENT.

KANIA, AG. C. J.—This is a reference made under Section 66 (1) of the Indian Income-tax Act by the Income-tax Appellate Tribunal. The material facts, as found in the statement of the case, are these. The late Bai Bhicaiji Dhunjibhoy appointed her husband and her son and three daughters as the trustees under her last will and testament, dated January 28, 1937. By clause 5 of that will it was provided as follows:—

"After deducting my death-bed and medical expenses and after payment of my debts, during the lifetime of my husband Dhunjibhoy Motabhoy Vakil, my trustees shall pay out of the net income of my movable and immovable properties such amounts as may be sufficient for the maintenance of my husband Dhunjibhoy Motabhoy Vakil, my daughter Motibai and my son Motabhoy Dhunjibhoy Vakil and the balance shall be accumulated and invested in Government Securities. During the lifetime of my husband Dhunjibhoy Motabhai Vakil my said husband, my daughter Motibai and my son Motabhoy shall have the right to use and occupy free of rent such portions of my immovable property at Warden Road as are now occupied by me and the other members of the family. Besides these three such of my children and grandchildren as may be invited shall alone have the right to reside and besides them none others shall be allowed to reside."

In pursuance of that provision, the parties named in the clause occupied the Warden Road property for the assessment year 1942-43. The trustees were sought to be assessed under the head of "income from property" in respect of this Warden Road bungalow. It was contended on their behalf that the trustees cannot be said to have realized any income whatsoever from the property in question which could be computed under Section 9, and, therefore, they were not liable to pay any income-tax in respect of this Warden Road property. The Income-tax Officer rejected that contention of the trustees but on appeal they succeeded before the Assistant Commissioner of Income-tax. The taxing authorities took the matter up to the Income-tax Appellate Tribunal and the Tribunal restored the order of the Income-tax Officer. The present reference is made at the instance of the trustees. The question submitted for the Court's consideration is in these terms:—

"Whether upon the facts found by the Tribunal, the annual value of the property on Warden Road, Bombay, has been rightly included in the assessment under Section 9 of the Income-tax Act?"

On behalf of the trustees it was argued before us that the Indian Income-tax Act was enacted with the object of taxing income. In the present case the trustees cannot by virtue of the express provision of clause 5 of the will let these premises to anyone and are obliged to give the bungalow for occupation to the persons named in the clause free of rent. It was therefore contended that there being no income, Sections 3 and 4 of the Indian Income-tax Act could not be relied upon to tax the annual letting value of this bungalow, as was sought to be done by the taxing authorities. It was argued that under Section 41 of the Indian Income-tax Act the liability of the trustees was only to be taxed to the same extent as the beneficiaries were liable to be taxed, and as the right to occupy premises did not amount to receipt of any income, the beneficiaries would not be liable to be taxed in respect of this right of occupancy. In this connection the assessees relied on *Tennant* v. *Smith*[1], and particularly on the following observation of Lord Halsbury, Lord Chancellor, at p. 157:—

"I am of opinion, in the words of Lord Young, that the thing sought to be taxed is not income unless it can be turned into money."

The assessees also relied on *Bejoy Singh Dudhuria* v. *Commissioner of Income-tax*[2] in support of their contention that when a sum of money is charged on the property such sum is not the income of the owner of the property although initially he receives the same.

On behalf of the Commissioner it was urged that this line of reasoning is incorrect. The only question to be considered under the Income-tax Act is: what is the income under the charging Sections 3 and 4? The expression there used is "total income" which is defined in Section 2 (15) of the Indian Income-tax Act in these terms:—

"'total income' means total amount of income, profits and gains referred to in sub-section (1) of Section 4 computed in the manner laid down in this Act."

Therefore to ascertain what is the total income, the Court must look at Sections 6 and 9 which contain the heads of income and how computation was to be made in respect of the head "income from property." It was argued that the scheme of the Income-tax Act was that once a party was shown to be the owner of a property, he must be taxed under the head "income from property" and the computation of the income must be in accordance with Section 9 of the Indian Income-tax Act. It was contended that the actual receipt of the rent in the hands of the owner is quite immaterial for the purposes of assessment. The law has laid down a

(1) [1892] A. C. 150. (2) [1933] 1 I.T.R. 135; 60 I.A. 196.

particular method of computation in respect of income from property and that must be applied to arrive at the figure to be inserted against the head "income from property" in the individual assessee's assessment.

In my opinion the contention of the trustees is not correct. The word "income" has not been defined in the Act, but for the purposes of the Indian Income-tax Act the expression "total income" is defined in Section 2 (15). The legislature has used there the words "computed in the manner laid down in this Act." Therefore in order to ascertain the total income of an assessee his income must be computed in the manner laid down in the Act and particularly Chapter III. In this connection the words used in Section 9 may be particularly noted. The section provides as follows:—

"The tax shall be payable by an assessee under the head 'Income from property' in respect of the *bona fide* annual value of property consisting of any buildings . . ."

The legislature has therefore expressly provided that the tax shall be payable by the assessee in respect of the *bona fide* annual value irrespective of the question whether he receives that value or not. Section 9 (2) provides that for the purposes of this section, the expression "annual value" shall be deemed to mean the sum for which the property might reasonably be expected to let from year to year. It is again significant to note that the word used is "might" and not "can" or "is." Reading these two paragraphs of Section 9 together, it is clear that the income from property is thus an artificially defined income and the liability arises from the fact that the assessee is the owner of the property. It is further provided in the section that if the owner occupies the property he has to pay tax calculated in the manner provided therein. Therefore, by reason of the fact that the property is not let out, the assessee does not escape taxation.

On behalf of the trustees it was argued that in the present case the trustees are prevented from letting out the property to anyone by virtue of clause 5 of the will itself. That, however, in my opinion, makes no difference. The liability to tax does not depend on the power of the owner to let the property, as it also does not depend on the capacity of the owner to receive the *bona fide* annual value of the property. The law has laid down an artificial rule by which the amount is to be considered the income of the assessee from immovable property and provided that he should be taxed on that footing. In my opinion the argument of the Commissioner on this point is correct.

The observation of Lord Halsbury, Lord Chancellor, in *Tennant* v. *Smith*[1], does not help the assessees. In that case the Court was concerned only with the liability of the occupant of the property to pay tax. On page 154 of the report at the bottom it is noted as follows:—

(1) [1892] A.C. 150, at p. 157.

"But the bald dry proposition that the mere fact of occupying a house, which house as property is already taxed, is not income in any sense, could, I think, hardly be disputed."

The Court, therefore, was considering the question of the liability of the occupant to pay tax in respect of a property the income of which was already taxed in the hands of the owner. That question does not arise for consideration here. It may be observed that the rules of taxation found in the Schedules annexed to the English Act are materially different from the rules of taxation contained in the Indian Income-tax Act. This has been noticed frequently by all Courts, and therefore it will not be proper to apply the observations made in respect of the liability of the occupant to pay tax under the English Act to the liability of the trustees, the owners of the property, under the Indian Income-tax Act. *Bejoy Singh Dudhuria* v. *Commissioner of Income-tax*[1] does not help the trustees because in that case the Court was not concerned with the taxation of income from immovable property. There it was a general question in respect of the income of the assessee and the Court decided that if in fact the income was charged with the payment of a certain sum and payment was made to satisfy that charge, the amount so paid was never the income of the assessee and could not be considered his income. The report of the case shows that the recipient of the amount was assessed on the amount received and that question was not before the Court. In this connection Mr. Setalvad drew our attention to *In the matter of the Official Assignee*[2]. In that case on the insolvency of a party a certain house became vested in the Official Assignee. That was the only property of the insolvent. The Official Assignee disputed his liability to be taxed under Section 9. The Court rejected that contention. At page 245, after noting the observations in *Commissioners of Inland Revenue* v. *Fleming*[3], the Court observed as follows:—

"In the present case the income was in the nature of statutory income arrived at upon the basis of the *bona fide* annual value of the property in question."

The objection of the Official Assignee was overruled on that ground. In my opinion that is the correct view of the liability of an owner to pay income-tax having regard to the combined effect of Sections 3, 4, 2(15), 6 and 9 of the Indian Income-tax Act.

Section 41 of the Indian Income-tax Act does not help the assessees because under that section two things have to be considered: first, the trustees become liable in the like manner and to the same amount as the tax would be leviable upon and recoverable from the beneficiaries; and, secondly, where the individual shares of the persons on whose behalf the income is receivable are indeterminate or unknown, the tax is orderedto

(1) [1933] 1 I.T.R. 135; 60 I.A. 196.
(2) [1937] 5 I.T.R. 233.
(3) (1928) 14 Tax Cas. 78.

be levied at the maximum rate. In India we have no distinction between legal and equitable estate. In *Currimbhoy Ebrahim Baronetcy Trust* v. *Commissioner of Income-tax* [1], the Judicial Committee of the Privy Council has held that the trustees in whom the property is vested are liable to be taxed under the Indian Income-tax Act. The extent of the liability is to be determined on the true interpretations of Sections 3, 4, 2 (15), 6 and 9 of the Indian Income-tax Act. The argument that under Section 41 the tax is to be levied in the like manner and in the same manner as to be recoverable from the beneficiaries does not help the assessees. If in the present case the ownership of this property is deemed to be vested in the beneficiaries, they could not avoid taxation on the ground that they themselves were occupying the property. It seems to me, therefore, that Section 41 of the Indian Income-tax Act does not help the assessees.

The question of rate of taxation is not relevant to the present discussion. If in making a settlement the settlor does not choose to define clearly the specific and individual shares of the beneficiaries, the assessment must be at the maximum rate. Whether the taxation should be at the highest rate or not is a matter of policy, with which we are not concerned. In my opinion, therefore, the answer to the question submitted to us is in the affirmative.

The assessees to pay the costs of the reference.

CHAGLA, J.—I agree. It is true that under the Indian Income-tax Act the only thing that can be taxed is income and nothing else. The charging section is Section 3; it charges the total income of an assessee; and "total income" is defined in Section 2 (15) as the total amount of income, profits and gains computed in the manner laid down in this Act. Before income can be computed in the manner laid down in the Act there must be income to which the mode of computation can be applied. Now it cannot be disputed that income from property is taxable income. The only question is: what is income from property or how is it to be computed? And for that purpose one must turn to Section 9 of the Indian Income-tax Act. The scheme of the Income-tax Act is that the income from property which is made liable to tax is not the actual income but an artificial or statutory income as defined in Section 9 and that artificial or statutory income is the *bona fide* annual value of the property. Therefore the fact that the owner of the property receives no income in fact or even that there is no possibility of his receiving an income is irrelevant for the consideration of the question as to what the artificial or statutory income of an assessee is from property. The test and the only test laid down in the Act is the *bona fide* annual value of the property, and in the case of every property that test can be complied with and the annual value of the property can be determined. Therefore what the Act does is to make the annual rental value of the property the

(1) [1935] 3 I.T.R. 395; 61 I.A. 209.

income of the owner of that property and it is that income that has got to be taxed under the Act.

I, therefore, agree with the learned Chief Justice that the answer to the question should be given in the affirmative.

Reference answered in the affirmative.

[IN THE BOMBAY HIGH COURT.]

COMMISSIONER OF INCOME-TAX

v.

SIR PURSHOTTAMDAS THAKURDAS.

SIR LEONARD STONE, C. J., and CHAGLA, J. November 14, 1945.

INDIAN INCOME-TAX ACT (XI OF 1922), SEC. 12 (2)—LITIGATION EXPENSES—INCOME FROM OTHER SOURCES—ELECTION AS DIRECTOR OF RESERVE BANK—LITIGATION EXPENSES INCURRED IN SUCCESSFULLY DEFENDING SUIT FOR SETTING ASIDE ELECTION—WHETHER ALLOWABLE DEDUCTION.

The assessee who was elected as a member of the Local Board of the Reserve Bank of India incurred in the year of account legal expense of Rs. 7,500 in successfully defending a suit brought some time after his election for a declaration that his election was invalid:

Held, (*i*) *that the expenditure was not capital in nature inasmuch as it was not an expenditure incurred in creating or in originating the source of income or in bringing it into being, but in preserving it when it was already there;*

(*ii*) *that the expenditure was incurred solely for the purpose of making or earning the income as a member of the Local Board of the Reserve Bank of India;*

(*iii*) *that the sum was therefore allowable as a deduction under Section 12 (2) of the Income-tax Act.*

Commissioner of Income-tax v. *Sir Homi M. Mehta* [*1943*] (*11 I.T.R. 142*) distinguished.

Cases referred to :—

Atherton *v.* British Insulated and Helsby Cables Ltd. ([1926] A.C. 205; 95 L.J.K.B. 336; 134 L.T. 289; 42 T.L.R. 187; 10 Tax Cas. 155).

Commissioner of Income-tax, Bihar and Orissa *v.* Sir Kameshwar Singh [1942] (L.R. 69 I.A. 15; 199 I.C. 314; 44 Bom. L.R. 778; A.I.R. 1942 P.C. 11; 10 I.T.R. 214: 8 B.R. 545).

Commissioner of Income-tax *v.* Sir Homi M. Mehta [1943] (11 I.T.R. 142).

Income-tax Appellate Tribunal, New Delhi *v.* Central India Spinning Weaving and Manufacturing Co., Ltd. [1943] (11 I.T.R. 266; I.L.R. 1943 Nag. 307).

Kangra Valley Slate Co. Ltd. *v.* Commissioner of Income-tax [1935] (16 Lah. 479; 7 I.T.C. 375; 37 P.L.R. 749; 3 I.T.R. 324).

Mahabir Parshad and Sons *v.* Commissioner of Income-tax [1945] (13 I.T.R. 340).

Southern *v.* Borax Consolidated Ltd. [1942] (10 I.T.R. Suppl. 1; [1941] 1 K.B. 111).

Vallambrosa Rubber Co., Ltd. *v.* Farmer ([1910] Sess. Cas. 519; 47 Sc. L.R. 488; 5 Tax Cas. 529).

Reference under Section 66 (1) of the Indian Income-tax Act (XI of 1922) by the Income-tax Appellate Tribunal: Income-tax Reference No. 18 of 1943.

STATEMENT OF CASE.

"This is a reference under Section 66 (1) of the Indian Income-tax (Amendment) Act, 1939, and is made on the application of the Commissioner of Income-tax, Central, Bombay, asking us to refer five questions stated to be questions of law arising out of our appellate judgment in Regular Assessment Appeal No. 36, Bombay, of 1942-43, for their Lordships' opinion. The application of the Commissioner of Income-tax and the written answer of the assessee are, respectively, Exs. A and B. A copy of our judgment is appended to this reference as Ex. C.

2. The short facts of this lengthy and laboured application are stated in paragraph 2 of our judgment, and may be restated for the purpose of this reference. Sir Purshottamdas Thakurdas who is the assessee in this case was a director of a number of limited companies in the year of account Samvat 1995. On November 12, 1935, he was elected a member of the Local Board for the Western Area of the Reserve Bank of India, which office is ordinarily held for five years. Some time after his election one Mr. P. D. Shamdasani brought a suit against him for a declaration that the election was invalid and that he himself should be declared duly elected. The suit was dismissed both in the first Court and appeal. In defending the suit the assessee incurred a legal expense of Rs. 7,500 in the year of account. These facts are undisputed.

3. The Income-tax Officer computed the total income of the assessee for the charge year 1940-41 at Rs. 7,67,343 which included Rs. 42,872 that the assessee had received as 'director's fees' in the year of account. He claimed a deduction of Rs. 7,500 from this amount as legal expense incurred by him as stated above. The Income-tax Officer rejected the claim holding that the expense was of a capital nature, and that it had been incurred for the purpose of acquiring or retaining the position of a director of the Reserve Bank of India. The assessee had returned the income from director's fees as income from 'other sources' assessable under Section 12 of the Indian Income-tax (Amendment) Act, 1939. Apparently, the Income-tax Officer based his order on Section 12 (2) of the Indian Income-tax Act which provides that the income of a person from 'other sources' shall be computed after making allowance for any expenditure (not being in the nature of capital expenditure) incurred solely for the purpose of making or earning such income, profits or gains, provided that no allowance shall be made on account of expenses described in clauses (a), (b) and (c) of the sub-section. In appeal, the Appellate Assistant Commissioner thought that the assessee's ordinary profession was to hold the position of a director of

the several limited companies. He therefore thought that Rs. 7,500 was a business expense within the meaning of Section 10 (2) (xii) of the Indian Income-tax (Amendment) Act, 1939, and allowed the claim. Relevant extract of the Income-tax Officer's order and a copy of the Appellate Assistant Commissioner's order are Exs. D and E.

4. The Department appealed to the Tribunal from the order of the Appellate Assistant Commissioner. In appeal, it was common ground that the assessee's income from director's fees was income from 'other sources.' It followed that an allowance such as the one claimed could only be made if the conditions laid down in Section 12 (2) of the Act were satisfied. The Department contended before us that the expense was of a personal nature. But we held that it was not, and that, on the contrary, it was an expense incurred for the purpose of retaining the assessee's position as a member of the Local Board of the Bank which position, in turn, enabled him to earn the income that he derived or expected to derive from his position as such member. We accordingly dismissed the Department's appeal holding that the assessee was entitled to claim the allowance under Section 12 (2) of the Act, and confirmed the Appellate Assistant Commissioner's order although on a different ground.

5. The Commissioner of Income-tax has formulated not less than five questions the first of which is:—

" Whether there was any evidence before the Tribunal to support the finding that the expenditure of Rs. 7,500 was 'incurred solely for the purpose of making or earning' an income."

A belief is generally held that a question formulated in an 'any evidence' form becomes a question of law even if it is substantially a question of fact. In this case at least, we cannot help remarking that the question is misconceived. There was no contest before us that the assessee was a member of the Bank and was deriving income. From this undisputed fact it was easy to infer that the legal expense incurred by the assessee for the purpose of retaining his seat was to secure such income. In his application the Commissioner conjectures certain motives of the assessee in retaining his position which, however, are not at all to the purpose. The second and the fifth questions are only repetitions of the first in different forms. We think therefore that these questions do not at all arise for reference.

6. The only material questions are Nos. 3 and 4. They really involve only one question for reference which we submit for their Lordships' opinion in the following form:—

Question referred.—' Whether, on the facts of the case, the legal expense of Rs. 7,500 incurred by the assessee in defending a suit brought to unseat him was rightly allowed as a deduction in computing his total

income for the charge year 1940-41, under Section 12 (2) of the Indian Income-tax (Amendment) Act, 1939 ?' "

M. C. Setalvad, for the Commissioner.

Sir Jamshedji Kanga with *M.M. Jhaveri* and *M.R. Mody*, for the assessee.

JUDGMENT.

STONE, C.J.—This is a reference under Section 66 (1) of the Indian Income-tax Act. The short question which the Tribunal has framed is as follows:—

"Whether, on the facts of the case, the legal expense of Rs. 7,500 incurred by the assessee in defending a suit brought to unseat him was rightly allowed as a deduction in computing his total income for the charge year 1940-41, under Section 12 (2) of the Indian Income-tax (Amendment) Act, 1939 ?"

The facts can be shortly stated as set out in the case. Sir Purshottamdas Thakurdas, who is the assessee in this case, was a director of a number of limited companies in the year of account Samvat 1995. On November 12, 1935, he was elected a member of the Local Board for the Western Area of the Reserve Bank of India, which office is ordinarily held for five years. Some time after his election one Mr. P. D. Shamdasani brought a suit against him for a declaration that the election was invalid and that he himself should be declared duly elected. The suit was dismissed both in the first Court and in the appeal Court. In defending the suit the assessee incurred a legal expense of Rs. 7,500 in the year of account. These facts are undisputed.

The relevant section of the Indian Income-tax Act under which head directors' fees come is Section 12 of the Act. Sub-section (2) provides:—

"Such income, profits and gains shall be computed after making allowance for any expenditure (not being in the nature of capital expenditure) incurred solely for the purpose of making or earning such income, profits or gains......................."

And then there is a proviso with regard to certain excluded matters.

Mr. Setalvad on behalf of the Crown has taken two points. The first is that the expenditure is a capital expenditure. In my opinion this is not so. It was not an expenditure incurred in creating or in originating the source of income or in bringing it into being, but in preserving it when it was already there. The expenditure was incurred in refuting the attack upon the directorship and might or might not be an expense which recurred at some future time. In my opinion the matter is really covered by the judgment of the Lord Chancellor, Lord Cave, in *Atherton* v. *British Insulated and Helsby Cables, Ltd.*[1] In that case the respondent company

(1) (1925) 10 Tax Cas. 155, at p. 192.

claimed as a deduction in computing its profits for income-tax purposes a lump sum of £ 31,784 which it had contributed irrevocably as the nucleus of a pension fund established by trust deed for the benefit of its clerical and technical salaried staff, that being the sum actuarially ascertained to be necessary to enable past years of service of the then existing staff to rank for pension, and it was held that the sum in question was not an admissible deduction in arriving at the company's profits for income-tax purposes. The Lord Chancellor said this :—

"But when an expenditure is made, not only once and for all, but with a view to bringing into existence an asset or an advantage for the enduring benefit of a trade, I think that there is very good reason (in the absence of special circumstances leading to an opposite conclusion) for treating such an expenditure as properly attributable not to revenue but to capital."

There is a decision of the High Court of Lahore to a contrary effect and, as it is a decision on the Income-tax Act which we have to construe, it is a case to which this Court will give the very closest attention: *Kangra Valley Slate Co., Ltd.* v. *Commissioner of Income-tax*[1]. In that case the assessees carried on the business of manufacturing slates and for this purpose had obtained under a lease the exclusive right of quarrying slate in a particular village. The proprietors of the village instituted a suit to eject the assessees and to restrain them by injunction from quarrying and the assessees incurred expenses of Rs. 13,397 in defending this before the Courts, and then the question was raised whether that came within the provisions of Section 10 (2) (ix) of the Indian Income-tax Act, and it was held that the expenditure incurred, being a non-recurring outlay required to retain a capital asset, was in the nature of capital expenditure.

I do not think it is essential to go into the judgment in that case, because the Court which decided it was made up of Mr. Justice Addison and Mr. Justice Sale and in a later case (*Mahabir Parshad and Sons* v. *Commissioner of Income-tax*[2]), when sitting as a member of a Full Bench, Mr. Justice Sale said of his previous decision that it was not intended to be an authoritative exposition of the question of what is or what is not capital expenditure. To the effect that such an expenditure is an income expenditure and not a capital one is also the case of *Income-tax Appellate Tribunal, New Delhi* v. *Central India Spinning, Weaving and Manufacturing Co., Ltd., The Empress Mills, Nagpur*[3]. On this first question, therefore, in my opinion on the authorities, which draw a clear distinction between the bringing into being of an asset and its maintenance and preservation, this case falls within the maintenance and preservation of an existing asset and, therefore, the appeal fails on this point.

(1) [1935] 3 I.T.R. 324; I.L.R. 16 Lah. 479.
(2) [1945] 13 I.T.R. 340.
(3) [1943] 11 I.T.R. 266; I.L.R. 1943 Nag. 307.

The second question which arises is whether the costs of this litigation were incurred "*solely*" for the purpose of making and earning the income. Various English cases have been examined in this Court, but the wording of the Schedule to the English Income Tax Act is very different and I do not think that any use is to be derived from them. Mr. Setalvad on behalf of the Crown submits that what the assessee did in defending this litigation was not only to secure his fees as a director but was also to secure the privileges attributable to that office and he points out that under Section 9 of the Reserve Bank of India Act, 1934, the members of the Local Board are given certain rights of franchise and other rights and he says that there is attached to the office of the director a status carrying certain privileges, the right for example to influence and shape the policy of the Reserve Bank and therefore the monetary policy of India.

The case of *Commissioner of Income-tax* v. *Sir Homi M. Mehta*[1] is also relied upon. Now the circumstances in that case were rather special, for the assessee who was the promoter, managing director and principal shareholder of a company made a gift of Rs. 3 lakhs to the company when it was in financial difficulties and he then claimed this sum as a deduction from his assessable income on the ground that if he had not made the gift the company would have failed and he would have lost his capital invested in the company, his salary, his business reputation and credit. The passage relied upon is at page 148 in which the learned Chief Justice, Sir John Beaumont, says this :—

"It seems to me quite impossible to say that this payment was made to the Company solely for the purpose of enabling the assessee to maintain his income derived from the Director's and Managing Director's fees and dividends on shares. The object of the expenditure must have been also to preserve the value of the other 75 per cent. of the shares in the Company which the assessee did not hold. If his sole purpose had been to preserve his income derived from that particular Company, obviously a more business-like arrangement would have been to make to the Company a loan, which could have been repaid to the assessee as a debt. But the main object was to keep the Company going, to maintain his own reputation as the man who had promoted the Company."

Mr. Setalvad further submits that a man of the status of the assessee did not defend this action solely for the purpose of getting his director's fees but also to maintain his status. On the other hand, the case for the assessee is put thus by Sir Jamshedji Kanga. He says that payment is not only for attending the directors' meetings but for services and duties performed and that what Mr. Setalvad points out as being privileges are in fact duties laid down by the Act which it is incumbent for the directors to

(1) [1943] 11 I.T.R. 142.

carry out. The Income-tax Act has no regard to status and privileges and does not quantify them in moneys; therefore, says Sir Jamshedji Kanga, what it taxes is the director's fees and the costs of the litigation are in defending those fees. It is also pointed out that it is a pure matter of speculation what was the assessee's motive in defending the action and further that there is no evidence at all on the record as to what that motive was other than to defend his directorship. In this respect it should be observed that in the proceedings the personal reputation and honour of the assessee were not attacked. Sir Jamshedji Kanga also relies upon the case of *Commissioner of Income-tax, Bihar & Orissa* v. *Sir Kameshwar Singh*[1]. In that case the assessee was a money-lender and he had lent a large sum of money to a company and he sued the company and obtained a decree. After that some of the shareholders of the company sued him for damages and that suit was decided also in favour of the assessee. Subsequently in making his return for income-tax for the year 1931-32 the assessee claimed to deduct the expenses incurred by him in defending the second suit under Section 10 (2) (ix) of the Indian Income-tax Act, 1922, and it was held by the Privy Council that the assessee's defence to the second suit was just as essential for the full protection of his rights as the creditor in the loan, as was his earlier suit for the recovery of the loan; and that therefore he was entitled to the deduction claimed, because the expenses were incurred by him solely for the purpose of earning the profits or gains of the money-lending business. Lord Thankerton in delivering the judgment of the Judicial Committee said:—

"It has to be remembered that money is the stock-in-trade of a money-lender. The appellant might well have come to a different conclusion, if he had realised the close connection of this loan with the transactions alleged in the Agra suit. If it really added anything, their Lordships would agree with the High Court that at least three of the other transactions referred to in the appellant's further statement of case provide evidence that the alleged transaction with the Agra United Mills was not foreign to the money-lending business of the respondent and his father.

Their Lordships are, therefore, of opinion that the facts stated by the Commissioner cannot justify the opinion expressed by him, but that the expenditure in question was incurred solely for the purpose of earning the profits or gains of the money-lending business, and that the High Court were right in holding the respondent entitled to the deduction claimed, and in answering the question of law asked by the Commissioner in favour of the respondent."

In my judgment the only purpose of incurring expenditure in this case was for the assessee to preserve his directorship. There was no personal

(1) [1942] 10 I.T.R. 214, at p. 218.

attack upon him which he was seeking to defend. What his own private motive, if any, in preserving his position as a director may have been does not seem to me to be relevant. So far as the Revenue Authorities are concerned, the directorship only sounds in fees and the only purpose of defending the action was to preserve the office and therefore the fees. Accordingly in my opinion the Crown fails on this question also. The Commissioner to pay the costs of the assessee.

CHAGLA, J.—I agree.

Two questions arise on this reference. The first is whether the expense incurred by Sir Purshottamdas Thakurdas in defending the suit filed against him by Mr. Shamdasani was incurred solely for the purpose of making or earning an income which he derived from being a member of the Local Board of the Reserve Bank of India; and the second question is whether such an expenditure was in the nature of capital expenditure.

Now in this case it cannot be disputed that Sir Purshottamdas Thakurdas incurred the expenditure for the purpose of earning the income as a member of the Local Board of the Reserve Bank. The question that we have got to determine is whether it was incurred solely for that purpose. Now whether it was solely incurred or not is essentially a question of fact, and we have to consider what are the findings of fact of the Tribunal as set out in the statement of the case. The first fact which has been found by the Tribunal is that Sir Purshottamdas defended this litigation in order that he should not be unseated as a member of the Local Board of the Reserve Bank; and the second finding of fact is that income was derived by Sir Purshottamdas as a member of the Local Board of the Reserve Bank and which is shown under Section 12 of the Indian Income-tax Act as having been derived from other sources. It is not disputed by Mr. Setalvad for the Department that the sole purpose of Sir Purshottamdas in fighting this litigation was to preserve his seat. It is not suggested that there were any personal allegations against him or that he was defending the suit for his personal honour or integrity. Once that is conceded and once it is found that the sole purpose of defending this litigation was to preserve his seat, and if it is also found that the seat yielded income, then it follows that the expenses of the litigation were incurred solely for the purpose of earning that income. It may be that Sir Purshottamdas' seat on the Board might not only have given him income but might have given him other rights and privileges. It might have given him a status and a position; but to my mind those are irrelevant considerations. The source which is taxed is the directorship, and if the litigation is fought for the sole purpose of preserving that source, then in my judgment it is immaterial what other benefits the assessee may derive from that particular source. The purpose and the sole purpose for incurring this expenditure was to preserve and maintain the

source which yielded the income which is shown as being derived from other sources under Section 12 of the Indian Income-tax Act. Mr. Setalvad has also argued that, looking to the provisions of the Reserve Bank of India Act, a director or a member of the Local Board not merely gets fees but also gets certain rights and privileges and he has certain functions and obligations to discharge. Now it is patent that Sir Purshottamdas was paid his fees as a director or a member of the Local Board for discharging the functions and obligations which were made incumbent upon him by the provisions of the Reserve Bank of India Act, and as such director or member he also enjoyed certain rights and privileges. That, to my mind, would be true of any office to which a salary or an emolument is attached. Every office not only gives to its holder a monetary remuneration but also confers upon him certain rights and privileges and also casts upon him certain duties and obligations. Therefore there is nothing peculiar about the position of a director of the Reserve Bank.

Mr. Setalvad has relied on a decision of our Court in *Commissioner of Income-tax* v. *Sir Homi M. Mehta*[1]. In that case Sir Homi Mehta made a gift of rupees three lakhs to a company of which he was the promoter, managing director and principal shareholder when that company was in financial difficulties and Sir Homi Mehta claimed that sum as a deduction from his assessable income on the ground that if he had not made the gift the company would have failed and he would have lost his capital invested in the company, his salary, and his business reputation and credit. Sir John Beaumont, Chief Justice, held that this sum of rupees three lakhs was not paid solely for the purpose of earning such income, profits or gains as required by Section 12, sub-section (2), of the Indian Income-tax Act. Now it is to be noted that both in the statement of the case and at the Bar when that case was argued it was conceded on behalf of the assessee that his sole purpose in making that gift was not to earn income as a director or to earn dividends on his shares but one of his objects—and the main object—was to save his business reputation. As was pointed out, Sir Homi Mehta felt that if the company failed 75 per cent. of the shareholders would lose and he having promoted the company he was actuated to make a gift of rupees three lakhs in order to save the company. On those facts only one decision was possible at which the Court arrived, namely, that the sum of rupees three lakhs paid by Sir Homi Mehta was not solely for the purpose required by Section 12, sub-section (2), of the Indian Income-tax Act. The difference between the case we have and the case which Sir John Beaumont, Chief Justice, and Mr. Justice Kania had before them is obvious and apparent. In this case the assessee has throughout maintained that his sole purpose in fighting the litigation was to earn the income as a member

(1) [1943] 11 I.T.R. 142.

of the Local Board of the Reserve Bank of India; and as I have pointed out, the Tribunal in their statement of the case have not found that the assessee had any other purpose than the purpose of earning the income. It would be entirely irrelevant to enter into the motives of Sir Purshottamdas why he fought this litigation. Mr. Setalvad has invited us into the attractive region of speculation. He wants us to consider what might have moved the assessee in defending his seat on the Local Board of the Reserve Bank. He asks us to speculate and to hold that Sir Purshottamdas might have thought of his honour, reputation, position and status as a member of that important body. But after all, as has been pointed out over and over again, we are merely an advisory body and we must advise on the facts found by the Tribunal. There is not even a suggestion that there was any other purpose on the part of the assessee for defending the suit, brought by Mr. Shamdasani except the pure business and monetary purpose of earning his fees as a member of the Local Board of the Reserve Bank. Sir Jamshedji Kanga at the Bar has reiterated and re-emphasised this purpose of his client, and as no other purpose appears on the face of the record we must accept that and hold that in this case the object and purpose with which this expenditure was incurred was solely, as required by Section 12, sub-section (2), of the Indian Income-tax Act, for earning the income as a member of the Local Board of the Reserve Bank of India.

The second question is whether this expenditure is in the nature of a capital expenditure, because if it is that, even though it was incurred solely for the purpose of earning the income, the assessee would not be entitled to claim the exemption. Mr. Setalvad has strongly relied, as he was entitled to, on the case of the Lahore High Court in *Kangra Valley Slate Co., Ltd.* v. *Commissioner of Income-tax*[1], and I admit that it is very difficult to distinguish that case from the facts of the case before us. If the principle enunciated in that case be a sound one, then, undoubtedly that principle applies to the facts of this case as well. In that case the assessees were carrying on a business of manufacturing slates and they had obtained a lease for the exclusive right of quarrying slate in that particular village. The proprietors of the village filed a suit to eject them, and the assessees resisted the suit and incurred an expense in doing so; and the question was whether they were entitled to claim the exemption with regard to that expense; and the Court held that the expenditure, being a non-recurring outlay required to retain a capital asset, was in the nature of a capital expenditure. In coming to that conclusion the Bench was largely influenced by an observation of Lord Dunedin in *Vallambrosa Rubber Co., Ltd.* v. *Farmer*[2]. The particular observation of Lord Dunedin which is set out in the judgment of the Lahore High Court is as follows:—

(1) [1935] 3 I.T.R. 324; I.L.R. 16 Lah. 479 (2) (1910) 5 Tax Cas. 529, at p. 536.

"... I think it is not a bad criterion of what is capital expenditure as against what is income expenditure to say that capital expenditure is a thing that is going to be spent once and for all, and income expenditure is a thing that is going to recur every year."

Now in this bald form this observation of Lord Dunedin seems to suggest that the only test to be applied in order to find out whether a particular expenditure is a capital or income expenditure is whether it is recurring or non-recurring in its character. Now, with respect to the learned Judges, it was hardly fair to the learned Law Lord to have quoted him in this incomplete fashion, because, when you turn to the judgment itself, we find that Lord Dunedin qualifies his remark by saying:—

"Now, I don't say that this consideration is absolutely final or determinative, but in a rough way I think it is not a bad criterion of what is capital expenditure as against what is income expenditure..."

Once this qualification and reservation is borne in mind, it would immediately be seen that what Lord Dunedin was laying down was one of the several tests which have got to be applied in order to determine what is capital expenditure and what is income expenditure. Fortunately it is not necessary for us to differ from a judgment of another High Court on an all-India statute because that very High Court seriously doubted the validity of that judgment when it came to be considered by a Full Bench of that High Court in *Mahabir Parshad and Sons* v. *Commissioner of Income-tax* [1], and although Mr. Justice Sale who was a party to both the judgments did not wholly repudiate his own judgment, he did say that his exposition of the question of what was and what was not capital expenditure was not an authoritative exposition as stated in the *Kangra Valley Slate Company's case*[2]. The most that one can say is that it remains an exposition but not an authoritative one. But to my mind the proper test as to what is capital expenditure is laid down in two English cases, one, *Atherton* v. *British Insulated and Helsby Cables, Ltd.*[3], and the other in the judgment of Mr. Justice Lawrence in *Southern* v. *Borax Consolidated Ltd.*[4] The observations of Viscount Cave in *Atherton's case*[3] have already been referred to in the judgment of the learned Chief Justice; and what is to be remembered is that Viscount Cave points out that the test to be applied in order to determine whether an expenditure is a capital expenditure is not merely that it should be non-recurring but it should be an expenditure to bring into existence an asset or an advantage for the enduring benefit of a trade. To maintain an existing asset or to preserve an existing asset is not enough. The expenditure must be to bring into existence an asset which did not already exist or a new advantage which must endure for the benefit of that particular business or trade.

(1) [1945] 13 I.T.R. 340.
(2) [1935] 3 I.T.R. 524.
(3) (1925) 10 Tax Cas. 155.
(4) [1942] 10 I.T.R. Suppl. 1.

Now in this case when Sir Purshottamdas Thakurdas defended Mr. Shamdasani's suit, the asset, *viz.*, the directorship or the seat on the Local Board of the Reserve Bank, already existed. All that he was doing was to preserve and maintain an already existing asset. It is not suggested that as a result of the litigation any new asset came into existence or he obtained any new advantage for the purpose of the directorship. I can also understand a case where an assessee has to fight a litigation for the purpose of perfecting his title. It may then be contended that to perfect one's title is to bring into existence a fresh advantage which did not exist before. But in this case the title of Sir Purshottamdas Thakurdas was already complete; he was merely resisting the attack of a litigant who was trying to unseat him; and having succeeded, he did not in any way improve his position or acquire any fresh benefit but merely succeeded in preserving and maintaining an asset which he already possessed.

Mr. Justice Lawrence also in *Southern* v. *Borax Consolidated, Ltd.*[1], observed that :—

" . . . where a sum of money is laid out for the acquisition or the improvement of a fixed capital asset it is attributable to capital, but that if no alteration is made in the fixed capital asset by the payment, then it is properly attributable to revenue, being in substance a matter of maintenance, the maintenance of the capital structure or the capital assets of the Company."

Therefore, according to this learned Judge, there must be an acquisition or an improvement of a fixed capital asset before an expenditure can be considered to be a capital expenditure; but if the expenditure is incurred merely for maintenance of a capital asset, then it is not a capital expenditure. If we were to apply this test to the facts of this case, as I have already pointed out, it cannot be contended that what Sir Purshottamdas was doing was anything more than trying to maintain his capital asset. It may be noted that in that particular case in which Mr. Justice Lawrence made these observations (*Southern* v. *Borax Consolidated Ltd.*[1]), a company acquired land in America for the purpose of its business. Subsequently an action was brought in the American Courts against the company claiming that the company's title to the land and buildings erected thereon was invalid, and in defending the action the company incurred costs amounting to £6,000 and odd, and it was this sum of £6,000 and odd that the company was claiming as an expenditure which it was entitled to have exempted from the application of the tax.

Sir Jamshedji Kanga has also drawn our attention to a Nagpur case, *Income-tax Appellate Tribunal, New Delhi* v. *Central India Spinning, Weaving and Manufacturing Company Ltd., The Empress Mills, Nagpur*[2].

(1) [1942] 10 I.T.R. Suppl. 1, at p. 5. (2) [1943] 11 I.T.R. 266; I.L-R. 1943 Nag. 307.

In that case the assessee company incurred a certain expenditure as legal expenses in connection with a suit which it had brought against another company to restrain the latter from using a trade mark to which the assessee had acquired exclusive right by long usage; and the Court consisting of Mr. Justice Niyogi and Mr. Justice Digby held that the expenditure was revenue expenditure and was allowable in computing the taxable income of the assessee company from the business. It will be noticed that what the company was trying to do was to preserve and maintain its most important capital asset, namely, the trade mark to which it had acquired exclusive right. Notwithstanding that, the Court came to the conclusion that the assessee was entitled to the exemption.

Now Mr. Setalvad has strongly relied for this point also on the judgment of our Court to which I have already referred, namely, *Commissioner of Income-tax* v. *Sir Homi M. Mehta*[1]. In that case the Court not only held that the sum of rupees three lakhs paid by Sir Homi Mehta was not solely for the purpose of earning an income but they also came to the conclusion that the expenditure was in the nature of a capital expenditure; and Sir John Beaumont, Chief Justice, came to that conclusion on the ground that one of the purposes for which that sum had been expended was the maintenance of the business reputation of the assessee. Now Mr. Setalvad has seized upon this observation of the learned Chief Justice and he argues that just as much as in that case so in this case also if moneys are spent for the maintenance of a capital asset then the expenditure is in the nature of a capital expenditure. Now reading the judgment of the learned Chief Justice as a whole, it is clear that he did come to the conclusion that when Sir Homi Mehta paid the sum of rupees three lakhs, his business reputation did not remain exactly the same after the payment as it was before and he in terms holds that the object of the payment was to enhance the reputation of the assessee and to avoid his being associated with a company which had failed. Therefore the assessee in that case, Sir Homi Mehta, obtained an advantage for an enduring benefit of his business or trade which brings the case within the definition of Viscount Cave in *Atherton* v. *British Insulated and Helsby Cables, Ltd.*[2], to which I have already referred. It cannot be said in this case that in succeeding in this litigation Sir Purshottamdas Thakurdas in any way enhanced his business reputation. His business reputation remained exactly where it was and all that he gained was that he succeeded in keeping the seat from which Mr. Shamdasani was trying to oust him.

Under the circumstances I agree with the learned Chief Justice that the Commissioner must fail on this reference and we should answer the question referred to us in the affirmative. Commissioner to pay the costs of the reference.

Reference answered in the affirmative.

(1) [1943] 11 I.T.R. 142.

(2) (1925) 10 Tax Cas. 155.

[IN THE CALCUTTA HIGH COURT.]

J. A. SHELLIM v. COMMISSIONER OF INCOME-TAX, BENGAL.

GENTLE and ORMOND, JJ.

January 22, 1946.

INDIAN INCOME-TAX ACT (XI OF 1922), SECS. 13, 66 (2)—REFERENCE—BANK CREDITS—INFORMATION AS TO SOURCE OF CREDITS NOT GIVEN—ASSESSMENT BASED ON ESTIMATE—LEGALITY—WHETHER A QUESTION OF LAW AROSE.

Where the assessee's bank accounts showed considerable credits for a period of one year and he did not give any information as to the sources of these credits and the Income-tax Officer acting under the provisions of Section 13 of the Income-tax Act allowed 2/3rd of the total amount of credits as expenses and made an assessment upon 1/3rd :

Held, *that the question whether the assessment was proper or not was one of fact and no question of law arose for directing the Tribunal to state a case under Section 66 (2).*

Application under Section 66 (2) of the Indian Income-tax Act (XI of 1922): Income-tax Reference No. 3 of 1945.

E. R. Meyer, for the assessee.

No one appeared for the Respondent.

JUDGMENT.

GENTLE, J.—This is an application by the assessee under Section 66 (2) of the Income-tax Act for an order requiring the Income-tax Tribunal to state a case and formulate questions for the opinion of this Court. It arises in the following circumstances. The year of account in question is 1940-41. The assessee made a return to the Income-tax Officer in which he included, as income under other sources (Section 12), "speculation Rs. 365-8-0." On being asked to justify that amount, he was totally unable to do so although in the return, the income is set out to an exact anna. The Income-tax Officer, on an examination, found that he had two banks, the Eastern Bank and the other, Lloyd's Bank. In the Eastern Bank there were two accounts and one at the latter bank. In one of the Eastern Bank accounts and the Lloyd's Bank account there were considerable credits for a period of one year; the total of the two amounted to Rs. 79,972. There also were debits. The assessee was asked the source of the credits and he made an affidavit to the effect that they were results of transactions in gambling on horse races and at the card table. There was no further information given. It would seem that the Income-tax authorities believed that he was a heavy gambler but the sources of the several credits, amounting to a large sum of money, were entirely in the assessee's hands

and he gave no information and there was no evidence from whom or from where those moneys had been received, nothing beyond his own *ipse dixit.* Eventually, after appeal by the assessee to the Appellate Assistant Commissioner, an assessment was made at Rs. 26,590 upon the above amounts representing about 1/3rd of the credits. This assessment was made pursuant to Section 13 of the Act which, in effect, authorises the Income-tax Officer to estimate the amount of an assessment; of course in doing so he must act in accordance with propriety. The assessee appealed to the Income-tax Appellate Tribunal which upheld the assessment and dismissed the appeal and upon being asked to state a case, pursuant to five questions put before it by the assessee, the Tribunal refused, expressing the opinion that no question of law arises.

In my opinion the Tribunal was perfectly correct. I can see no point of law whatever arising here. Undoubtedly there were considerable proceeds which were credited in the bank accounts of the assessee. He gave no information whatever of the sources of those credits. All information was entirely in his hands and, I would express it, he withheld that information. There being nothing before the Income-tax Officer, so far as the sources of those receipts were concerned, he was obliged to act under the provisions of Section 13 and in doing so he has allowed 2/3rd of the total amount of the credits towards, what might be called, expenses and made an assessment upon 1/3rd. He was doing the best that he could in the circumstances. If the assessee had not withheld all information but had produced some evidence regarding the accounts and his gambling transactions then perhaps a different assessment might have been made. This was a pure question of fact and there is nothing to show that the Income-tax Officer in any way acted inconsistently with the provisions of Section 13. That being so, I cannot see that any question of law arises and in my opinion this application should be dismissed.

ORMOND, J.—I agree.

Application dismissed.

[IN THE CALCUTTA HIGH COURT.]

TARAK NATH BAGCHI

v.

COMMISSIONER OF INCOME-TAX, BENGAL.

GENTLE and ORMOND, JJ.

January 4, 1946.

INDIAN INCOME-TAX ACT (XI OF 1922), SECS. 22, 64, 66 (2)—JURISDICTION—PLACE OF ASSESSMENT—CONCURRENT JURISDICTION—BUSINESS

HAVING SEVERAL BRANCHES—TRANSFER OF CASE FROM ONE OFFICER TO ANOTHER ON ASSESSEE'S REQUEST AND NOTICE ISSUED BY LATTER OFFICER—RETRANSFER ON REQUEST—SUBSEQUENT ASSESSMENT WITHOUT ISSUE OF NOTICE—VALIDITY—APPELLATE TRIBUNAL—WHEN CAN BE REQUIRED TO STATE CASE—SCOPE OF SEC. 64.

The effect of sub-sections (1) and (4) of Section 64 is that, where two or more Income-tax Officers have territorial jurisdiction in respect of the same income, they exercise concurrent jurisdiction in the matter of issuing notices to the assessee and where notices have been issued by one officer it is unnecessary for the other officer to issue the same notices again. Sub-section (3) of Section 64 applies only when a question arises as to the place of assessment and when there is no dispute between the assessee and the Income-tax Officer as to the proper place of assessment the point need not be referred to the Commissioner under that sub-section.

The applicant was the receiver appointed by the High Court in respect of the assets of a business B & Co. which had several branches in Calcutta including one within the area of the Income-tax Officer of District No. 1 (2) and another within the area of the Income-tax Officer of District No. 5. Originally the officer of District No. 1 (2) had in his jurisdiction the assessment of the profits of the business. In October 1935, after the applicant became the receiver, the income-tax file was transferred from District No. 1 (2) to District No. 5 at the request of a pleader acting for the person at one time in charge of the business. In July 1936, the officer of District No. 5 issued a notice under Sections 34/22 (2) of the Income-tax Act upon the Hindu undivided family of B & Co. for submission of a return in respect of the profits of the business which should have been assessed during the year 1935-36. In January 1937 the applicant wrote to the officer of District No. 5 stating that the case should be transferred to the officer of District No. 1 (2) inasmuch as all accounts were kept in the office which was within the jurisdiction of the officer of District No. 1 (2). The transfer was effected and in June 1939 the Additional Income-tax Officer of that District made an assessment without issuing a fresh notice :

Held, *(i) that as the transfer was effected on express request, Section 64 (3) did not apply ;*

(ii) that the transfer from District No. 1 (2) to District No. 5 was a proper transfer, that the officer of District No. 5 had jurisdiction to issue the notice, that the notice issued in the name of the Hindu undivided family was valid inasmuch as it was served on the applicant and he had accepted it and that the officer of District No. 1 (2) had jurisdiction to make the assessment without issuing a fresh notice.

Even if any point of law arose upon which the Tribunal refused to state a case, if the High Court is satisfied that the decision of the Tribunal

is correct, no direction should be given for stating a case under Section 66 (2).

Bisheshwar Nath & Co., In re [1942] (10 I.T.R. 103) followed.

In the matter of an application under Section 66 (2) of the Indian Income-tax Act: Income-tax Reference No. 3 of 1943.

M. N. Ghosh and *S. D. Ghosh*, for the assessee.

S. K. Gupta and *J. C. Pal*, for the Commissioner.

JUDGMENT.

GENTLE, J.—The applicant is the receiver appointed by this Court in respect of the assets of a business which was conducted in the name of Messrs. P. M. Bagchi & Co. There are several branches of this business at various places in Calcutta including one at No. 19 and 19/1, Gulu Ostagar Lane, and another at No. 14, Clive Street, Calcutta; the former is within the area of the Income-tax Officer of District No. 1 (2) and the latter within the area of the Income-tax Officer of District No. 5. It is said that the principal place of business was at Gulu Ostagar Lane, Calcutta. Proceedings having been taken with respect to this business of which, at one time, a man named Panchanan Bagchi was the sole proprietor and the applicant having been appointed receiver, he entered upon his duties and took possession of the assets on the 18th July, 1935.

In this matter before us, the Commissioner of Income-tax, Calcutta, is showing cause against a rule nisi granted by this Court on the 12th January, 1944, requiring the Income-tax Tribunal to refer to this Court certain questions which the applicant alleges arose out of its decision with regard to the assessment of the profits of the business for the year 1935-36. The questions with which the rule nisi is concerned relate to the notice given under Sections 34/22 (2) of the Indian Income-tax Act and to the assessment made upon the notice. There also arises, in connection with those questions, consideration of the transfer by one Income-tax Officer to another officer of the file relating to the assessment of the profits of the business.

Originally, the Income-tax Officer of District No. 1 (2) had in his jurisdiction the assessment of the profits of the business. This, it is stated was because the business premises in that District were the principal place of business. In October, 1935, after the present applicant became receiver, the Income-tax Officer of District No. 1 (2) was requested by Mr. J. R. Roy, a pleader, to transfer the income-tax matters relating to the business to District No. 5. Mr. J. R. Roy at that time was instructed by Mr. Panchanan Bagchi who at one period was in control of the business. On the 23rd July, 1936, the officer of the District No. 5 issued a notice under Sections 34/22 (2) in respect of the profits of the business; it was, in fact, issued upon the Hindu undivided family known as P. M. Bagchi & Co. This

notice required a return to be made in respect of the profits of the business which should have been assessed during the year 1935-36. Nothing seems to have been done, although apparently reminders or notices were sent by the Income-tax Officer until the 20th January, 1937, when the applicant wrote to the Income-tax Officer of District No. 5 acknowledging a post-card and stating that his office was at No. 19 and 19/1, Gulu Ostagar Lane, Calcutta, where all the accounts were kept and books of account were being produced to the Income-tax Officer of District No. 1 (2). In view of those circumstances, the applicant requested a transfer of the pending case to District No. 1 (2) for his convenience. This transfer was effected and the file was sent to District No. 1 (2). On the 22nd June, 1939, the Additional Income-tax Officer of that District made an assessment against which the applicant appealed to the Tribunal and in respect of which the present matter arises.

It was contended that the two transfers, firstly, from District No. 1 (2) to District No. 5 and, later, from District No. 5 back to District No. 1 (2), were without authority and invalid; consequently, the notice given under Sections 34/22 (2) by the Income-tax Officer of District No. 5 was bad and invalid, and further that the assessment subsequently made by the Additional Income-tax Officer of District No. 1 (2) could not stand, since it was made firstly, upon an invalid notice, secondly, without any notice having been given, and thirdly, by an officer who had no jurisdiction to make the assessment, and it was also faintly suggested that the notice issued by the officer of District No. 5 was a bad notice as it was addressed to a Hindu undivided family.

The principal argument arises upon the provisions of Section 64 of the Indian Income-tax Act. These are as follows:—

"(1) Where an assessee carries on a business,..............at any place, he shall be assessed by the Income-tax Officer of the area in which that place is situate or, where the business....................is carried on in more places than one, by the Income-tax Officer of the area in which the principal place of his business,............................is situate.

* * *

(3) Where any question arises under this section as to the place of assessment, such question shall be determined by the Commissioner.........

(4) Notwithstanding anything contained in this section, every Income-tax Officer shall have all the powers conferred by or under this Act on an Income-tax Officer in respect of any income, profits or gains accruing, or arising or received within the area for which he is appointed."

It was argued that since the principal place of business was at the address within the area of District No. 1 (2), the Income-tax Officer of that District alone had jurisdiction to give notice under Section 34 of the Income-tax Act and also that Section 64 in no way allows a transfer of the

file from one officer to another, save when such transfer is made by the Commissioner. The effect of Section 64 and its sub-sections has been considered in *In re, Bisheshwar Nath & Co.*[1], a decision by the Allahabad High Court. It was there held that the effect of sub-sections (1) and (4) of Section 64 is that, where two or more Income-tax Officers have territorial jurisdiction in respect of the same income, they exercise concurrent jurisdiction in the matter of issuing notices to the assessee and where notices have been issued by one officer it is unnecessary for the other officer to issue the same notices again. Sub-section (3) of Section 64 applies only when a question arises as to the place of assessment and when there is no dispute between the assessee and the Income-tax Officer as to the proper place of assessment the point need not be referred to the Commissioner under that sub-section.

With respect I agree with that decision. In the present case there was no question of dispute at any time between the assessee and the Income-tax authorities as to the proper place of assessment. Originally, a request was made by a pleader, acting for the person at one time in charge of the business, for the income-tax file to be transferred from District No. 1 (2) to District No. 5. Later, in reply to a request by the applicant the file was retransferred from District No. 5 back to District No. 1 (2). In my view, a request by the assessee for transfer is not a question arising as to the place of assessment. Sub-section (3) refers to a position when a contest exists as to the correct assessment area; it does not apply when there is an express request, as it was made here for the assessee's own convenience, that a particular Income-tax Officer should take charge of the matter of income-tax assessment. The transfer from District No. 1 (2) to District No. 5 was a proper transfer, the officers in each District having concurrent jurisdiction, and that thereafter the Income-tax Officer of the latter District had jurisdiction to issue the notice which, in fact, he did under Section 34 of the Act. There is no doubt that that notice was served upon the applicant. Although it was in the name of the undivided family of P. M. Bagchi & Co., it related to the business of which the applicant was a receiver. No exception whatever was taken to the notice or to its form. Indeed, the applicant in his letter of the 20th January, 1937, makes it quite clear that he had accepted the notice and the matters with regard to assessment were acceptable to him and in that letter he merely asked that the case should be transferred to District No. 1 (2) for his own convenience, inasmuch as the books of the business were kept at the place of business in that area and were then being shown to and examined by the Income-tax Officer of District No. 1 (2). There is no substance whatever in the objection raised to the name by which the assessee was

(1) [1942] 10 I.T.R. 103.

indicated in that notice. The Additional Income-tax Officer of District No. 1 (2) merely continued the assessment which had been initiated by the officer in District No. 5 and he assessed the profits of the business pursuant to the notice given by the Income-tax Officer of District No. 5. There was jurisdiction in the Income-tax Officers of each of those Districts to deal with the profits and income-tax to be assessed upon those profits, inasmuch as there was a business carried on at addresses in those two Districts and therefore under sub-section (4) of Section 64 each Income-tax Officer had authority to deal with the profits of the business in their respective areas. That being so, each would have concurrent jurisdiction, as indicated in the Allahabad case, to issue a notice and when one of those officers issued a notice the other officer could act upon it without giving a fresh notice.

It was contended that, assuming the correctness of the transfer, and that the matters of assessment could have been dealt with in the area of District No. 1 (2), since the Additional Income-tax Officer has made the assessment, the assessment must be bad. I am unable to appreciate that argument. There is an Additional Income-tax Officer in District No. 1 (2). He is properly authorised to deal with income-tax matters within that District and in doing what he did he acted clearly within the authority and jurisdiction which he is entitled to exercise.

This application is made under Section 66 (2) of the Income-tax Act, inasmuch as the Appellate Tribunal was asked to state a case for the opinion of this Court on questions which are now being considered and the Tribunal refused to state the case. This sub-section, so far as it is material, provides as follows:—

"If on any application being made under sub-section (1) the Appellate Tribunal refuses to state the case on the ground that no question of law arises, the assessee or the Commissioner, as the case may be, may, within six months from the date on which he is served with notice of the refusal, apply to the High Court, and the High Court may, if it is not satisfied of the correctness of the decision of the Appellate Tribunal, require the Appellate Tribunal to state the case and to refer it . . ."

It is only when this Court is not satisfied of the correctness of the decision of the Appellate Tribunal that it should be required to state a case. I am of opinion that the decision of that Tribunal was correct. Even if any point of law arose upon which the Tribunal refused to state the case nevertheless the Tribunal's decision being correct, no direction should be given for stating a case. That is the position, in my view, which arises here.

Before I conclude, I desire to make reference to the petition which the applicant solemnly affirmed on the 3rd February, 1943. It was on the contents of that petition that the rule nisi was issued by this Court. The petition contains more than one, what I would describe as gross mis-statement

f facts. In paragraph 11, it is stated that by a letter written by the etitioner on the 20th January, 1937, he intimated to the Income-tax)fficer of District No. 5 that the business in question was, at all material imes, carried on at No. 19 and 19/1, Gulu Ostagar Lane, within the jurisdicion of District No. 1 (2). The paragraph continues:—

"It was pointed out that the statement made by Mr. J. R. Roy, pleader, o the effect that the business was carried on at 14, Clive Street, was not only mauthorised but totally untrue and without any foundation."

This letter, or a copy of it, was not exhibited to the petition. It has een exhibited to the letter of the Commissioner regarding the rule nisi. [have already referred to that letter but will do so again. In that letter the pplicant wrote as follows:—

"........my office being at No. 19 and 19/1, Gulu Ostagar Lane, Calcutta, and all the accounts are kept at the said address and moreover the books of accounts of 1339 B. S. are to be produced to the Income-tax Officer, District No. 1 (2), as per his notice.

In view of the above circumstances, I ask you to transfer the pending case of this company to the District No. 1 (2) for my convenience.

Hope to be favoured with the same and oblige."

In that letter there is no reference whatever to the principal place of business being at No. 19 and 19/1, Gulu Ostagar Lane, Calcutta, nor to any statement by Mr. J. R. Roy regarding the place where the business was carried on being untrue and without foundation. The letter is quite clear. The applicant was informing the Income-tax Officer that his own office, that is to say, the receiver's office, was at the address given and where all the books were kept and that is why he wished the file to be transferred to the District Officer having jurisdiction over the place where the books were kept. It is unfortunate that this solemnly affirmed petition should contain such gross mis-statements.

In conclusion, it is desirable to emphasise that the transfer which followed the applicant's letter to the Income-tax Officer of the 20th January, 1937, was made solely to suit his convenience, and at his request. Nevertheless it has been argued that what was done was without any authority or right. In my view, this application is devoid of all merits and should be dismissed.

ORMOND, J.—I agree.

Application dismissed.

[IN THE PATNA HIGH COURT.]

THE PROVINCE OF BIHAR *v.* F. R. HAYES AND OTHERS.

FAZL ALI, C. J., MANOHAR LALL and SINHA, JJ.

January 28, 1946.

BIHAR AGRICULTURAL INCOME-TAX ACT (VII OF 1938), SEC. 11—ASSESSEES INHERITING SPECIFIC SHARES OF PROPERTY APPOINTING AGENT TO MANAGE PROPERTY—WHETHER AGENT ASSESSABLE UNDER SEC. 11 ON AGGREGATE INCOME RECEIVED BY ASSESSEES—SCOPE OF SEC. 11—" BENEFICIARY," " LAND "—MEANINGS OF—STATEMENT OF CASE—MUST BE DRAWN UP BY BOARD.

The assessees were fifteen persons who had inherited specific shares in an estate in a district from a lady. They resided in different parts of the world and each of them had executed at different times a general power of attorney in favour of P. authorising him to manage the property which devolved upon him upon the death of the lady. The question was whether the income received by the assessees should be added together and the aggregate amount should be taxed in the hands of P. under Section 11 of the Bihar Agricultural Income-tax Act:

Held, (*i*) *that the definition of "beneficiary" as given in the explanation to Section 11 must be held to be controlled by its accepted legal meaning and that the section could not have been intended to apply to income received by full owners of property through their servant, agent or manager ;*

(*ii*) *that the word " land " in Section 11, being singular, must be taken to apply to one unit of agricultural property and not to a number of separate and independent properties and that as each of the assessees held a separate share in the estate and each share formed an independent unit of agricultural property by itself, each of them was entitled to the whole income of the property held by him and not merely to a portion of the income derived from that property* ;

(*iii*) *that therefore Section 11 did not apply to the assessees.*

The language of Section 11 strongly suggests that it was meant to apply to those cases where land is held by a trustee or someone whose position in relation to the land is similar to that of a trustee.

Under Section 25 (2) of the Bihar Agricultural Income-tax Act, the statement must be drawn up and referred to the High Court by the Board and not by someone representing the Board.

Statement of Case under Section 25 (2) of the Bihar Agricultural Income-tax Act (VII of 1938) by the Board of Agricultural Income-tax, Bihar, dated the 29th May, 1943, regarding assessment of agricultural income-tax on Mr. F. R. Hayes and others of Purnea: Miscellaneous Judicial Case No. 73 of 1943.

STATEMENT OF CASE.

"Case stated under Section 25 (2) of the Bihar Agricultural Income-tax Act, 1938 (VII of 1938), at the instance of the assessees, Mr. F. R. Hayes and others of Purnea and elsewhere, referring a question of law arising from the order on their appeal against assessment for the year 1941-42.

2. The petitioners are 15 persons who inherited shares in an estate in Purnea from Mrs. Hayes. They reside in different parts of the world and each of them has at different times from 1925 onwards executed a general power of attorney in favour of Mr. Picachy. They were assessed to agricultural income-tax for the year 1941-42 on a net agricultural income of Rs. 27,556 by the Agricultural Income-tax Officer, Darbhanga Circle, under the provisions of Section 11 of the Act. This section provides that if a person holds land from which agricultural income is derived partly for his own benefit and partly for the benefit of beneficiaries, or wholly for the benefit of beneficiaries, agricultural income-tax shall be assessed on the total agricultural income derived from such land at the rate which would have been applicable if such person had held the land exclusively for his own benefit; and the explanation to the section defines 'beneficiary' as a person entitled to a portion of the agricultural income derived from the land. A copy of the order of the Agricultural Income-tax Officer, dated the 8th May, 1942, is enclosed (Exhibit A).

3. The assessees appealed to the Assistant Commissioner of Agricultural Income-tax of Purnea on the ground that the joint assessment made on Mr. Picachy as the petitioners' manager and holding general powers of attorney was illegal and not maintainable as the petitioners hold distinct and separate properties as would appear from the return filed and from the copy of Register 'D' filed with the objection petition. It was further urged that as the shareholders had individually authorised Mr. L. Picachy to work for them by distinct and separate powers of attorney and at different times, they never formed an association of individuals, and that their individual income being far short of Rs. 5,000 they were not liable to be taxed. A copy of the appeal petition, dated the 3rd June, 1942, is enclosed (Exhibit B).

4. According to the Assistant Commissioner of Agricultural Income-tax, Purnea, as Mr. Picachy is holding the land wholly for the benefit of the beneficiaries, his case falls under Section 11 of the Act. He, therefore, dismissed the appeal. A copy of his order, dated the 20th July, 1942, is enclosed (Exhibit C).

5. The assessees then filed a petition under Section 24 before the Commissioner of Agricultural Income-tax, Bhagalpur Division, against this order on the ground that Section 11 of the Act under which joint assessment was made was not applicable to the present case, inasmuch as the person

contemplated in Section 11 must be either a common manager, administrator or executor or in any other capacity recognized by law. It was also contended that the individual income of each of the petitioners being much below Rs. 5,000 the order of assessment was without jurisdiction and that the orders passed by the lower Courts were liable to be set aside. A copy of the revision petition, dated the 18th August, 1942, is enclosed (Exhibit D).

The Commissioner dismissed the revision petition as in his opinion the word 'hold' in Sections 11 and 12 covered Mr. Picachy's possession and management. A copy of his order, dated the 12th January, 1943, is enclosed (Exhibit E).

6. The assessees then filed an application before the Bihar Board of Agricultural Income-tax under Section 25 (2) of the Act, formulating the following question of law for reference to the High Court :—

'Whether an individual, holding separate powers of attorney from different proprietors regarding their respective specific shares in the estate, can be said to be holding the land within the meaning either of Section 11 or of Section 12 of the Bihar Agricultural Income-tax Act, 1938.'

A copy of the application, dated the 9th March, 1943, is enclosed (Exhibit F).

7. The Board considered that Section 12 does not apply and decided that part of the question in favour of the assessees, but refers to the High Court the question whether an individual holding separate (*sic*) respective specific share in the estate can be said to be holding the land within the meaning of Section 11 of the Bihar Agricultural Income-tax Act, 1938. The Board is of opinion that the individual in question, Mr. Picachy, is holding the land for the benefit of persons entitled to a portion of the agricultural income derived from the land. The fact that he is in possession is hardly denied but it is argued that as there is no community of interest between the actual proprietors, their separate income should not be 'lumped together' for purposes of assessment. The law however appears to the Board to make Mr. Picachy liable to assessment on the total agricultural income of all the proprietors whose attorney he is irrespective of whether their shares are separate or not. A copy of the Board's resolution dated the 22nd April, 1943, is enclosed (Exhibit G)."

Dr. P. K. Sen and *M. K. Mukherjee*, for the assessees.

Advocate-General and *Government Pleader*, for the Province of Bihar.

JUDGMENT.

FAZL ALI, C.J.—This is a reference by the Board of Agricultural Income-tax, Bihar, under Section 25 (2) of the Bihar Agricultural Income-tax Act (VII of 1938). The question which the assessees asked the Board to refer was framed on their behalf in these words :—

"Whether an individual, holding separate powers of attorney from different proprietors regarding their respective specific shares in the estate, can be said to be holding the land within the meaning either of Section 11 or of Section 12 of the Bihar Agricultural Income-tax Act, 1938."

The Board in submitting the question to this Court has expressed the following opinion (See Board's resolution dated the 22nd April, 1943) :—

"It seems to the Board that there is no question of law involved in the application of Section 12 which certainly does not apply to the present case but that there is a question of law whether Section 11 applies to the manager on behalf of a number of shareholders, each share being separate and distinct and separately recorded in the collectorate registers. A reference will be made to the High Court on this point."

The assessees in the present case are 15 persons who inherited specific shares in an estate in Purnea from one Mrs. Hayes. They reside in different parts of the world and each of them has executed a general power of attorney in favour of one Mr. Picachy authorising him to manage the property which devolved upon him upon the death of Mrs. Hayes. The incomes received by the various assessees have been set out in the following schedule which is printed at page 3 of the paper-book :—

Serial No.	Names of proprietors.	Extent of shares.							Amount of profits.		
		A.	G.	C.	K.	D.	R.	J.	Rs.	As.	P.
1	F. R. Hayes, Esqr.	1	17	3		1			3253	1	6
2	John Kissock Hayes		18	3	1	2			1626	8	9
3	Mrs. Mary Affleck Hayes		18	3	1	2			1626	8	9
4	Mrs. L. M. Jelbart	1	17	3		1			3253	1	6
5	Miss. M. N. Hayes	1	17	3		1			3253	1	6
6	Mrs. M. E. Betteley	1	17	3		1			3253	1	6
7	Mrs. V. G. Dickinson	1	17	3		1			3253	1	6
8	Mr. G. P. Cammiade		6	1	2	2	6	2	558	2	1
9	Mr. P. F. Cammiade		6	1	2	2	6	2	558	2	1
10	Mr. T. B. Cammiade		6	1	2	2	6	2	558	2	1
11	Mrs. A. M. Fellowes		18	1	1				1578	11	4
12	Mr. A. H. W. Bentinck		12	2	1		6	2	1084	5	10
13	Mr. D. W. Bentinck		12	2	1		6	2	1084	5	10
14	Mrs. A. W. Perrie		12	2	1		6	2	1084	5	10
15	Mrs. G. Holyoak		17	3		1			1530	13	10
					Total			...	27555	9	7

The real question to be decided in this reference is whether the 15 assessees should be assessed on their separate incomes or the income received by them should be added together and the aggregate amount should be taxed under Section 11 of the Act. The contention put forward on behalf of the assessees is that their income cannot be lumped together for the purpose of assessment and that they are not liable to be assessed at all because the individual income of each assessee is less than Rs. 5,000. They

point out that it is most unjust that persons whose income is just a little over Rs. 1,000 or Rs. 500 should be assessed at all or assessed at rates applicable to more than 25 to 50 times these figures respectively. The schedule shows that in the year of accounting three of the assessees had received Rs. 558 each; three Rs. 1,084 each and the highest income received by any of the assessees did not exceed Rs. 3,253 odd. The assessees' contention has been negatived by the Agricultural Income-tax authorities and it has been held that their case is covered by Section 11 of the Act and the aggregate of their incomes in the hands of Mr. Picachy is liable to assessment under that section.

It has been conceded on behalf of the Department that the assessees have no community of interest with each other, that they reside in different countries such as England, East Africa, India etc., and that Mr. Picachy was appointed by them at different times and under different powers of attorney and it is a mere coincidence that he is the holder of a power of attorney on behalf of all the assessees. But it has been held that the terms of Section 11 are wide enough to cover a case like the present and to justify the assessment of the total agricultural income. Section 11 runs thus:—

"(1) Save as provided in Sections 9, 12 and 13, if a person holds land from which agricultural income is derived partly for his own benefit and partly for the benefit of beneficiaries or wholly for the benefit of beneficiaries, agricultural income-tax shall be assessed on the total agricultural income derived from such land at the rate which would have been applicable if such person had held the land exclusively for his own benefit, and the agricultural income-tax so payable shall be assessed on the person holding such land, and he shall be liable to pay the same.

(2) Any person holding such land shall be entitled, before paying to any beneficiary the amount of agricultural income which such beneficiary is entitled to receive from the agricultural income derived from such land, to deduct the amount of agricultural income-tax at the rate at which the agricultural income is or will be assessed under sub-section (1).

Explanation.—In this section 'beneficiary' means a person entitled to a portion of the agricultural income derived from the land."

In my opinion the language of the section strongly suggests that it was meant to apply to those cases where land is held by a trustee or someone whose position in relation to the land is similar to that of a trustee. Trust has been defined by Sir Arthur Underhill in his well-known treatise relating to the Law of Trust and Trustees as follows:—

"Trust is an equitable obligation, binding a person (who is called a trustee) to deal with property over which he has control (which is called the trust property) for the benefit of persons (who are called the beneficiaries)

of whom he may himself be one, and any one of whom may enforce the obligation."

Another well-known definition of trust is to be found in the Indian Trusts Act and it runs as follows :—

"A 'trust' is an obligation annexed to the ownership of property, and arising out of a confidence reposed in and accepted by the owner, or declared and accepted by him, for the benefit of another or of another and the owner:

the person who reposes or declares the confidence is called the 'author of the trust': the person who accepts the confidence is called the 'trustee': the person for whose benefit the confidence is accepted is called the 'beneficiary': the subject-matter of the trust is called 'trust property' or 'trust money': the 'beneficial interest' or 'interest' of the beneficiary is his right against the trustee as owner of the trust property: and the instrument, if any, by which the trust is declared is called the 'instrument of trust.'"

It is true that there is no express reference to trust property in Section 11, but one who is familiar with the legal conception of a trust cannot fail to observe that the words used in Section 11 have a strong resemblance to those which are used in the two definitions. Trust may be express or implied or constructive but the common feature of all trusts is that (1) there should be a person who has possession or custody of some property, (2) there should be a person or persons for whose benefit the property is held by the former, and (3) there must be an obligation annexed to the ownership of the property for the benefit of another or another and the owner. The person who is entitled to certain benefits in the property is described as a beneficiary. This well-known legal expression has been defined in Wharton's Law Lexicon as follows :—

"A person having the beneficial enjoyment of property of which a trustee, executor etc., has the legal possession, in which sense it is gradually superseding the old term *cestui que trust.*"

This is the accepted legal sense in which the expression "beneficiary" is commonly used and I have no reason to think that it could have been intended to be used in an entirely different sense in this section. It is true that the explanation to the section purports to define the term "beneficiary" and states that the expression means "a person entitled to a portion of the agricultural income derived from the land." But this definition cannot be taken to be exhaustive or complete. The framers of the Act must be assumed to have known the accepted legal meaning of the expression and also known that the term "beneficiary" in law is not generally used with reference to a full legal owner but with reference to a person who has "beneficial interest" in some property which is usually in the possession

and control of another person. The distinction between beneficial interest and legal ownership is one of the most notable features of a trust and in my judgment "beneficiaries" referred to in Section 11 are those persons who have merely beneficial interest in a property, while the legal ownership of the property vests in a person or persons who hold the property for their benefit.

In the present case Mr. Picachy is merely an agent of the assessees and not the legal owner of the property, whereas every one of the assessees is the full legal owner of a distinct unit of property over which he has complete dominion. He is something more than a beneficiary, because he is not merely entitled to receive the income of the property but he can deal with it in any way he likes. He has also power to remove his agent whenever he likes and either take over the management of the property himself or appoint another agent to manage it. It is elementary that such a person is not a mere beneficiary of the property in the accepted sense of the term and as I have already observed I do not think that the accepted sense is excluded by the definition which is to be found in the explanation to Section 11 of the Act. Apart from its legal meaning even in ordinary use the expression "beneficiary" is seldom employed with reference to a full owner. In the Oxford Dictionary its meaning is stated to be "one who receives benefits or favours; a debtor to another's bounty." Even according to this meaning a beneficiary would be a very different person from a full owner who has complete dominion over his property and whose right is not limited to mere enjoyment of a certain part of the income of the property. It follows that an owner cannot become a beneficiary merely by executing a power of attorney in favour of another person authorising him to manage his own property. Therefore my conclusions are (1) that the definition of "beneficiary" as given in the explanation to Section 11 must be held to be controlled by its accepted legal meaning, otherwise it will be too wide and will cover persons who could not have been intended to be dealt with in that section, and (2) that the section could not have been intended to apply to income received by full owners of property through their servant or agent or manager.

Even if we assume for the purpose of this reference that Section 11 may be given the meaning which has been given to it by the Board, there would still be considerable difficulty, in my opinion, in applying it to the present case because of the fact that the word "land," which is used in Section 11 being singular, must be taken to apply to one unit of agricultural property and not to a number of separate and independent properties. In the present case each assessee holds a separate share in the estate and each share forms an independent unit of agricultural property by itself. Therefore in law each assessee holds a different property. From

this it must necessarily follow that Mr. Picachy is the holder of 15 different properties (which we may refer to as properties A, B, C, D, etc.) belonging to 15 different persons. It is not disputed that the owner of each property, that is to say, each of the present assessees, is entitled to the whole income of the property which is held by him, that is to say, one assessee is entitled to the whole income derived from A; another assessee is entitled to the whole income derived from B and the next assessee is entitled to the whole income derived from C and so on. As each share forms a separate unit of property, none of the assessees is entitled merely to a portion of the agricultural income derived from that property and therefore in the present case the assessees do not come within the definition of the word "beneficiary" as given in the section. That Section 11 will not be applicable to a case like the present may be illustrated by a a more obvious example. Let us suppose that Mr. Picachy was appointed to manage a certain property on behalf of X in the district of Patna; another property on behalf of Y in the district of Muzaffarpur and a third property on behalf of Z in the district of Darbhanga, X, Y and Z having nothing to do with each other and being separate owners of these properties. I do not think that in such a case the language of Section 11 would justify the assessment of the aggregate agricultural incomes of these three persons X, Y and Z derived from the properties in three different districts, merely because they happen to be managed by the same person. The difficulty in the way of such assessment will, as I have already indicated, be created by the use of the word " land " which obviously means one distinct unit of property. The word " land" will not apply to three different and independent estates belonging to three different persons in different parts of the province. X, Y and Z would not be hit by Section 11 because they would be respectively entitled to the whole income derived from their respective estates in Patna, Muzaffarpur and Darbhanga and would not therefore be included in the definition of " beneficiary " which means a person entitled to a portion of the agricultural income.

If Section 11 was not intended to apply to the case covered by the illustration, it could not have been intended to cover the present case because, as I have already said, though by coincidence the assessees have become entitled to specific shares in the same estate, yet each share constitutes a distinct unit of property and their case is not distinguishable in principle from that of a number of owners having different estates in different parts of the province.

I would, therefore, while recognising that Section 11 is somewhat clumsily drafted and therefore seems at first sight to be capable of being construed in the manner in which it has been construed by the Board, hold that according to its true meaning it cannot be held to apply to the

assessees concerned in this reference. I would, therefore, upon the facts stated in the reference answer the question which has been referred to us in the negative.

When this reference was put up before us it was brought to our notice that the statement of the case which was submitted to us under Section 25 (2) purported to have been signed only by the Secretary to the Board of Revenue. At that time we were constrained to point out that Section 25 of the Act clearly contemplated that the statement must be drawn up and referred to the High Court by the Board and not by someone representing the Board. We had to take notice of the sudden departure from the usual practice because it was the common feature of several references and in one case at least the statement which was submitted to the Court did not bear the signature of any person with the result that no one could say who had drawn up the statement. Fortunately the learned Advocate-General realised that the statement was not in order and necessary corrections have been made. We hope that in future the statements will be drawn up and submitted to this Court in conformity to the provisions of the Act under which the statements are to be submitted. The assessees are entitled to the costs of the reference which are assessed at Rs. 250 and they are also entitled to a refund of Rs. 100 deposited by them.

MANOHAR LALL, J.—I agree.

SINHA, J.—I agree with my lord, the Chief Justice.

Reference answered in the negative.

[IN THE BOMBAY HIGH COURT.]

BHIMJI R. NAIK *v.* COMMISSIONER OF INCOME-TAX, BOMBAY.

SIR LEONARD STONE, C. J., and KANIA, J. March 12, 1946.

INDIAN INCOME-TAX ACT (XI OF 1922), SEC. 4-A (b)—RESIDENCE OF FIRM—TEST—SITUATION OF CONTROL AND MANAGEMENT—QUESTION OF FACT OR LAW—DE FACTO CONTROL AND MANAGEMENT NECESSARY—"WHOLLY SITUATED," MEANING OF.

The control and management mentioned in Section 4-A (b) of the Indian Income-tax Act must be de facto control and management and not de jure control and management.

A liberal meaning is to be given to the words "wholly situated" and it must be ascertained in every case where in fact the control and management of the business is situated apart from the temporary journeyings of the active partners or the residence of the dormant ones.

In the case of a firm the problem ought to be approached from the same angle as in the case of a company.

Whether or not a man exercises control over a particular business may be a mixed question of law and fact.

One B. R. Naik carried on business in South Africa. In 1912 he returned to British India leaving his business in the hands of three managers. In 1937 he executed a deed styled as a partnership deed by which he admitted the three managers as partners having a share in profits and losses but retained to himself the full control of the business and even the right to dismiss any of the three partners. B. R. Naik however stated in an affidavit that he had not at any time either controlled and managed or attempted to control and manage the affairs of the business in South Africa. Two of the partners also filed affidavits stating that they had been carrying on the business of the firm without receiving any instructions from B. R. Naik. A summary of the correspondence made by the examiner of the Income-tax Department stated that B. R. Naik had left the control and management in the hands of the partners and that he only kept himself in touch just to caution them, while they informed him about the general condition of trade prevailing there. The Income-tax Appellate Tribunal arrived at the conclusion that the control and management of the firm was not situated wholly without British India and that the firm was therefore resident in British India :

Held, *that there was no evidence to support the conclusion of the Appellate Tribunal and that the firm was not resident in British India within the meaning of Section 4-A (b) of the Indian Income-tax Act.*

Income-tax Reference No. 6 of 1944.

This reference originally came up for hearing before Sir Leonard Stone, C. J., and Kania, J., on the 29th of September 1944 and the learned Judges sent the reference back to the Tribunal to record their finding on the question where the control and management of the business was situated: *vide* [1945] (13 I.T.R. 124). The Tribunal re-submitted the case after taking further evidence.

FURTHER STATEMENT OF CASE.

" The above case has been sent back to us by the High Court in order to record our finding of fact whether the control and management of the business were wholly situated abroad or not. We have taken further evidence on the question and we re-submit the case to the High Court of Bombay under Section 66 of the Indian Income-tax Act.

2. The assessee firm of Messrs. Bhimji R. Naik consists of four partners. Three of them reside in South Africa, and Rao Bahadur B. R. Naik, the capitalist partner, resides in British India. The firm carries on business in Salisbury, in South Africa. Rao Bahadur B. R. Naik went to Africa somewhere in 1902 and started the business. He stayed there for a period of ten years and returned to India in about 1912, when he was about 30 years of age. Thereafter he led a retired life. Since his return to India

the work is being carried on by three employees as managers. Up to 1937, the relations between the said managers and Rao Bahadur B. R. Naik were that of employees and an employer. In that year Rao Bahadur B. R. Naik took into partnership the managers who used to be his previous employees. No capital was introduced by the three partners. They were entitled to a certain share in the profits. There is only one office in South Africa and the three employees are named as managers both prior to the execution of the partnership deed and after. Besides the facts stated above, the following other evidence has been produced by the assessee and it is claimed that the control and management of the affairs of the above firm were situated wholly without British India :—

(1) A letter has been filed from a bank in South Africa, dated 17th November, 1944. It states that Rao Bahadur B. R. Naik never operated upon the bank account since 1912. Firstly, there is no evidence that this was the only bank with which the applicant firm used to deal. Secondly, it only shows that the position of Rao Bahadur B. R. Naik as regards this bank account has remained the same since 1912. Prior to 1937, the management of the firm in South Africa was carried on by the employees under the supervision and direction of the proprietor. This letter is produced for the first time after the remand by the High Court.

(2) The Income-tax Officer asked Rao Bahadur Naik to produce his correspondence file for the relevant accounting period between him and the South African office. It is stated that this correspondence file was originally produced before the Income-tax Officer and that it cannot now be traced. We find from the records of the case that some sort of correspondence file was produced by the assessee's representative before the Income-tax Officer. There is a note in the hand of the examiner which reads as follows :—

"Mr. Chhaganlal M. Desai, clerk of the assessee, and Mr. B. D. Jokhakar, registered accountant, attend and produce the following :—

1. Correspondence between the assessee and M/s. Bhimji R. Naik, Salisbury, South Africa, wherein he is a partner, and vice versa. Dates of correspondence 8-12-37 to 6-1-40 and 14-1-38 to 18-10-39.

2. Correspondence between M/s. Bhimji R. Naik, Salisbury, and M/s. Harilal Manilal & Co., of 346, Kalbadevi Road, Bombay—dates 13-6-38 to 18-10-39.

3. Letter from M/s. Harilal Manilal & Co., of 346, Kalbadevi Road, Bombay, dated 4-5-40.

The first set of correspondence shows that the nature of the correspondence is most formal informing the assessee on the one hand the general condition of business at Salisbury and always consoling the assessee in India not to worry at all for the business there. The assessee at the same

time in his turn and in his usual style has asked them to be very cautious and careful in the business.

The second set of correspondence is produced to convince the Department that the manager-partners at Salisbury give orders directly or indent goods as per the demand there to the firm at Bombay who sends the bills of lading, invoices etc., to Salisbury direct. The goods are ordered out without any consultation with the assessee partner here. Lastly, a letter from M/s. Harilal Manilal & Co., is produced testifying the whole fact mentioned in the preceding para.

After going through some of the letters it is seen that the assessee has left the management and control of the business at Salisbury in the hands of the partners at Salisbury. He only keeps himself in touch just to caution the partners at Salisbury, while the partners at Salisbury inform the assessee about the general condition of trade prevailing in Salisbury."

3. The assessee has not produced the correspondence file now. Surely, it was not difficult for him to obtain copies of the correspondence from his South African office even if the file in India was misplaced or lost. It appears from the examiner's note that the South African office used to continuously inform Rao Bahadur B. R. Naik about the general condition of the business and used to impress upon the managers the importance of being cautious and careful. One fact is however clear that the assessee was not taking any part in making purchases and sales of the business. Management and control of a business is not confined to making purchases and sales only. No reference was ever made by the assessee to this note of the examiner when the case was first heard by us.

4. There is an affidavit from two of the partners of the firm of Messrs. Bhimji R. Naik. In this affidavit, it is stated that they have been carrying on the business of the firm without receiving any instructions from Sardar Rao Bahadur B. R. Naik. Here we may mention that the examiner's note which was made when the correspondence was first produced before the Income-tax Officer shows that Rao Bahadur B. R. Naik was impressing upon the managers the desirability of being cautious and careful. So it is not quite correct to say that the partners in South Africa were not receiving any instructions whatsoever from Rao Bahadur B. R. Naik. We are not quite sure if these managers (partners) mean anything more than taking part in purchases and sales when they mention the words "control and management."

5. There is an affidavit of Manilal Rayaram which goes to show that the purchases were made by the firm in South Africa and no orders were received from Rao Bahadur B. R. Naik. This fact, in our opinion, is correct.

7. Lastly, we have the partnership deed before us. The relevant clauses have been reproduced in our appellate order.

8. Clause 2 appears to us to be rather peculiar. It states that the managers shall not be disclosed as partners in the said business and as far as the public is concerned they shall be held out as managers of the business. Clause 9 restricts the powers of the managers as regards changing of the premises of the business. That could only be done with the prior consent and approval of Rao Bahadur B. R. Naik. Clause 11 gives Rao Bahadur B. R. Naik complete right of dismissal as if the partners were his employees. Clause 14 states that B. R. Naik retains full control of the business and the managers are only there to carry out such instructions as are given to them from time to time by B. R. Naik. In our opinion, it is very likely that Rao Bahadur B. R. Naik left definite instructions in detail with the managers. He was continuously informed that his instructions were being carried out. He was therefore satisfied and it was not necessary for him to give any further orders or directions. B. R. Naik alone had the right to liquidate or close the business. Clause 15 provides that B. R. Naik should get 50% of the profits even though the managers had to employ another person at a higher salary. Such extra expense had to be met by the managers themselves. Under clause 18, B. R. Naik had the right to give the managers power of attorney. We have no evidence before us to show that such power of attorney was not granted. Considering clause 2 which provides that the managers should not be given out in the public to be partners, it is very likely that the managers used to get power of attorney from B. R. Naik.

9. Taking into account all the evidence produced before us we are of the opinion that Rao Bahadur B. R. Naik did as a matter of fact exercise some control over the management of the affairs of the firm in the relevant accounting period. The control and management of the firm was therefore not situated wholly without British India. We are of the opinion that the assessee firm is a firm resident in British India."

Sir Jamshedji Kanga, for the assessee.

M. C. Setalvad, for the Commissioner.

JUDGMENT.

STONE, C. J.—This reference was before this Court on the 29th of September 1944 when we decided that upon the true construction of sub-section 4-A (b) of the Income-tax Act, which deals with the question of residence of a Hindu undivided family, firm or other association of persons, the control and management therein mentioned must be de facto control and management and not de jure control and management and we sent this matter back to the Tribunal to find the necessary facts (see *B. R. Naik* v. *Commissioner of Income-tax*[1]). The assessee firm in this case admittedly carries on its business in South Africa. The suggestion of the Commissioner

(1) (1945) 13 I.T.R. 124.

was and is that Rao Bahadur Naik, who founded the business and returned to live in India, still retains the control and management of its affairs. Sub-section (b) of Section 4-A of the Income-tax Act provides :—

"For the purposes of this Act—

(b) A Hindu undivided family, firm or other association of persons is resident in British India unless the control and management of its affairs is situated wholly without British India."

Sub-section (c) deals with the case of a company and provides :—

" A company is resident in British India in any year if the control and management of its affairs is situated wholly in British India in that year, or."

There follows another proviso which is not material.

Control and management of the affairs of a business must be effected through the media of human minds, and in dealing with a plurality of persons who either jointly or severally exercise powers of control and management over a particular business, and who may be either generally or from time to time in different places and in communication by letter, telephone or telegram, it may be difficult to ascertain where the control and management is situated. Especially is this so, when, as in this case, the section refers to the control and management being situated wholly without British India. In one sense an American business man, who pays a short visit to this country and while here by cablegram gives some instructions to his firm in America, could be said to make his firm resident in British India for income-tax purposes. But in my opinion the canons of construction do not demand the conclusion of any such extreme result. I think that a liberal meaning is to be given to the words " wholly situated " and that it must be ascertained in every case where in fact the control and management of the business is situated, apart from the temporary journeyings of the active partners or the residence of the dormant ones. Some assistance is to be gained by comparing the language of sub-section (b) with that of sub-section (c), which deals with companies, and which I have already quoted. A company has a registered office and its directors hold their board meetings and its members their annual general meetings at a particular place. These are indications which must assist in any consideration of the situation of the control and management of a company, and free it from some of the difficulties which arise in the case of a firm. However in the case of a firm, the problem ought, in my opinion, to be approached from the same angle.

If this is correct, the further facts found by the Tribunal present little difficulty to our holding that this firm was managed and controlled outside British India. There are on record three affidavits, one of which is deposed to by Rao Bahadur Naik himself, he having died during the pendency of these proceedings, and in that affidavit he says :—

"The said business and its affairs are solely and wholly controlled and managed by the partners residing in South Rhodesia. I have not at any time either controlled and managed or attempted to control and manage the affairs of the said business and the control and management of the affairs of the said business are situated wholly without British India."

Then there is another affidavit by two of the three South African partners and they say :—

"We have never received any instructions from Sardar Rao Bahadur Bhimbhai R. Naik as to the purchases or sales or any matters of the firm and we have never referred to Sardar Bhimbhai R. Naik as to the management and conduct of any of the business affairs of the firm."

Lastly there is an affidavit by Mr. Manilal Rayaram who is the senior partner of a firm with whom the assessee firm do business and he says that he had purchased their goods for the last 20 years :—

"My firm has never and does not refer to Sardar Rao Bahadur Bhimbhai R. Naik about any matters of Messrs. Bhimji R. Naik in general and for the execution of the orders and for the payments received from Messrs. Bhimji R. Naik in particular. He also never interfered in any matters of the firm. The total purchases of Messrs. Bhimji R. Naik for the year ended 31st March 1939 done through my firm amount to about Rs. 29,900."

These affidavits remain unchallenged and no request was made or direction given to cross-examine the deponents upon them. Mr. Setalvad on behalf of the Commissioner has pointed out that by the effect of Section 106 of the Evidence Act when any fact is especially within the knowledge of any person, the burden of proving that fact is upon him. Unchallenged by any cross-examination, I think the affidavits to which I have referred do discharge the initial burden of proof.

The difficulty, however, arises because at the end of their further statement of the case the Tribunal has said this :—

"Taking into account all the evidence produced before us we are of the opinion that Rao Bahadur B. R. Naik did as a matter of fact exercise some control over the management of the affairs of the firm in the relevant accounting period. The control and management of the firm was therefore not situated wholly without British India. We are of the opinion that the assessee firm is a firm resident in British India."

In my opinion not only is that conclusion contrary to the evidence, but there is no factual evidence at all to support it. Whether or not a man exercises control over a particular business may be a mixed question of law and fact, for example, suppose that the dormant partner has given a mandate to the bank to honour the cheques drawn by the active partners, it could be argued that every time a cheque is drawn, the powers of the dormant

partner are being invoked. Whether that is so or not must be a question of law. The evidence of the facts with regard to the actions of the partners in this case is, it seems to me, all one way and that is against the exercise of control by B. R. Naik. The mere fact that he had the power of control, whilst it is a relevant consideration, is no evidence by itself of any fact of control or management and it is the acts and not the powers with which we are concerned. In my opinion, therefore, the question referred to us should be answered in the negative. It follows that the Commissioner must pay the costs. Commissioner to pay the costs of this hearing and of the previous hearing on which the remand was made.

KANIA, J.—I agree.

When the matter was first argued before us, it appeared that the Tribunal had come to its conclusion against the assessee on the construction of the deed of partnership. The rights of the partners, as defined by the deed of partnership, could give no answer to the question, whether the control and management were wholly outside British India. We therefore remanded the matter under Section 66 (4) of the Indian Income-tax Act for a further finding of facts.

The question whether the control and management are wholly outside British India is to be answered on the facts ascertained by the Tribunal. Before the matter was remanded, the Tribunal had before it three affidavits. The effect of those affidavits has been set out in the judgment of the learned Chief Justice. The contents of these affidavits were not challenged. It appears to be common ground also that after 1912 Rao Bahadur Naik never went to South Africa. If so, the only way in which the control or management could in fact be exercised by him would be either by letters, telegrams or telephones. The affidavits filed by two partners living in Africa and Rao Bahadur Naik negative the suggestion of any such directions being sent after the partnership was formed. The correspondence file was produced before the examiner, Income-tax Office. It appears that after the preliminary inquiry and assessment order was made, no importance was attached to this file. Rao Bahadur Naik died pending these proceedings and five years have elapsed since then. The non-production of the file by the legal representatives of Rao Bahadur Naik, when the matter was reconsidered on remand, under the circumstances, can be easily understood and no adverse inference could be drawn from that fact. The matter, however, does not leave room for much doubt. A summary of the correspondence made by the examiner of the Income-tax Department was produced before the Tribunal and it contained the following statement:—

"After going through some of the letters it is seen that the assessee (Rao Bahadur Naik) has left the management and control of the business

at Salisbury in the hands of the partners at Salisbury. He only keeps himself in touch just to caution the partners at Salisbury, while the partners at Salisbury inform the assessee about the general condition of trade prevailing in Salisbury."

The first part of this statement clearly indicates that the control and management were wholly at Salisbury. The latter part only deals with advices received from one end by the other. They would be natural in the case of a partner who has a share in profits and losses. They, however, do not lead to any conclusion about the control and management of the business.

When the case was remanded, the Tribunal in different paragraphs considered the facts relevant to the question to be answered. The first was a letter from the bank in South Africa. That indicated that since 1912 Rao Bahadur Naik had not operated on the banking account at all. The Tribunal sought to use this as leading to the inference that the management still remained in Rao Bahadur Naik, because between 1912 and 1937 he was the sole owner. I do not see any justification for that conclusion. Rao Bahadur Naik being the owner up to 1937 all acts done on his behalf, in law, must be presumed to be under his authority. In law he had the sole control and management. His agents could act only under his directions. That position was entirely changed when the partnership was entered into. It is therefore improper to draw an inference about the state of affairs after the partnership agreement was made, on the footing of the facts as they existed before. No inquiry was made as to how the account was operated upon after 1937. No explanation was asked and in my opinion there is no justification for holding that the same state of affairs, in respect of the right to operate on the account, continued as before.

In the second paragraph of the further statement of the case a summary of the correspondence leading to the conclusion, which I have quoted above, is made. In the third paragraph the Tribunal dealt with the question of sales and purchases. They held that in fact no business was carried on by the firm in British India and the sales and purchases were made wholly on instructions received from Africa and Rao Bahadur Naik had nothing to do with the same.

In paragraph 4 they considered the affidavits filed before. In that paragraph they also considered the effect of the note of the examiner, in relation to Rao Bahadur Naik's letter advising the South African partners to act with caution. Those words are treated as words of instructions. In my opinion, that is not the correct interpretation of the note made by the examiner.

As regards the affidavits of the two partners in South Africa, the Tribunal put a meaning on the words different from what they plainly bear.

The Tribunal thought that when the partners used the words "control and management," they probably meant "sales and purchases." The affidavits show that the partners, apart from sales and purchases, have separately stated that they received no instructions for anything else from Mr. Naik.

Paragraphs 5, 6 and 7 deal with the affidavits and do not contain any further finding.

Paragraph 8 deals with the clauses of the partnership agreement in the first instance. The next statement is as follows:—

"In our opinion, it is likely that Rao Bahadur B. R. Naik left definite instructions in detail with the managers."

In my opinion that inference is drawn without any materials or evidence before the Tribunal. They have not recorded any fact from which such inference could be justified. The next sentence is this:—

"He was continuously informed that his instructions were being carried out."

Again, for this there is no evidence whatsoever in the further statement of facts submitted by the Tribunal. There is no question of continuous information and there is no evidence of any instructions being carried out.

The last statement in that paragraph is in respect of the power of attorney. In my opinion there is no justification for holding that a power of attorney was granted by Rao Bahadur Naik to the partners in South Africa after they entered into the partnership agreement. There is no evidence that because they were described as managers to outsiders any power of attorney was required. It is well-known that munims carry on unlimited business even though they hold no power of attorney. As regards the bank, there is no evidence that a power of attorney was required. There is no evidence in whose name the account stands and under what circumstances the bank allows the partners in Africa to operate on the banking account. I therefore think that no inference in respect of the control and management of the business could be based on the footing of any power of attorney in the present case.

Apart from these, no other facts are recorded in the further statement of the case submitted by the Tribunal. The analysis of the statement of case made above, in my opinion, clearly shows that the conclusion of the Tribunal that Rao Bahadur Naik as a matter of fact exercised some control over the management of the affairs of the firm in the relevant accounting period is based on no evidence and therefore I agree that the answer to the question submitted for our opinion should be in the negative.

Reference answered in the negative.

[IN THE BOMBAY HIGH COURT.]

COMMISSIONER OF INCOME-TAX

v.

BIPIN SILK MILLS LTD.

SIR LEONARD STONE, C. J., and KANIA, J. November 3, 1944.

EXCESS PROFITS TAX ACT (XV OF 1940), SEC. 2 (21) (a)—COMPANY—DIRECTORS HAVING "CONTROLLING INTEREST"—SOME SHARES HELD BY DIRECTOR AND OTHER PERSONS AS TRUSTEES—WHETHER COMPANY DIRECTOR-CONTROLLED.

The assessee company had a share capital divided into 100 shares of Rs. 5,000 each. 43 shares were held by the directors in their individual names. 20 shares stood in the joint names of a director N and four other persons in their capacity as trustees. Under the trust deed N had an overriding power to decide questions in the management of the trust and the trustees must act as directed by N. The articles of association provided that if N was present at a meeting, as between the company and the shareholders, he had a right to vote as he pleased. The question was whether the assessee company was a director-controlled company within the meaning of Section 2 (21) (a) of the Excess Profits Tax Act:

Held, *that it was not necessary that the interest contemplated by Section 2 (21) (a) should be beneficial interest, that the trustee's interest was sufficient to bring the case within the meaning of that sub-section, that N had a controlling interest in respect of the 20 shares and that therefore the assessee company was a director-controlled company.*

J. Bibby and Co. v. *Commissioners of Inland Revenue* (*[1944] 1 All E. R. 548*) followed.

Cases referred to :—

J. Bibby and Co. *v.* Commissioners of Inland Revenue ([1944] 1 All E. R. 548).

British American Tobacco Co. *v.* Inland Revenue Commissioners [1942] (10 I.T.R. Suppl. 67).

B. W. Noble Ltd. *v.* Commissioners of Inland Revenue [1926] (12 Tax Cas. 911).

Case stated under Section 66 (1) of the Indian Income-tax Act (XI of 1922) by the Income-tax Appellate Tribunal: Income-tax Reference No. 19 of 1944.

The following facts are taken from the judgment of the Income-tax Appellate Tribunal.

"The Bipin Silk Mills Ltd., has a paid-up capital of 100 shares of Rs. 5,000 each. During the relevant accounting period there were four directors of the company. Besides the shares held by the directors in their individual names, 20 shares stand in the joint names of five persons in the register of the company :—

1. Nanji Kalidas,
2. Mrs. Nanji.

3. Sardar Tribhowandas Jagjivandas,
4. Raja Pandit Anandpuriyaji Atmaramji, and
5. Rajya Ratna H. M. Wadia.

Nanji Kalidas' name stands first and he is a director of the company. It is common ground that if it is held that these 20 shares are held by a director then the company would be a company in which the directors have controlling interest within the meaning of Section 2 (21) (a) of the Excess Profits Tax Act and the assessee would be entitled to compute his standard profits at 12 per cent. on the capital, as against 10 per cent.

The Excess Profits Tax Officer held that as these shares are not held by Nanji Kalidas in his individual capacity but as a trustee they cannot be treated as the shares held by the director for the purpose of ascertaining whether the company is a director-controlled company under Section 2 (21) of the Excess Profits Tax Act. The learned Appellate Assistant Commissioner upheld the order of the Excess Profits Tax Officer on the ground that in the case of these 20 shares which stand in the joint names, Nanji Kalidas, the director, has not the beneficial ownership.

We may here reproduce three relevant articles of the company :—

Article 7.—Save as herein otherwise provided the company shall be entitled to treat the registered holder of any share as the absolute owner thereof and accordingly shall not except as ordered by a Court of competent jurisdiction or as by statute required be bound to recognise any equitable or other claim to or interest in such share on the part of any other person.

Article 12.—The certificate of shares registered in the names of two or more persons shall unless otherwise directed by them be delivered to the person first named on the register.

Article 62.—Where there are joint registered holders of any share, any one of such persons may vote at any meeting, either personally or by proxy in respect of such share as if he were entitled thereto and if more than one such joint holders be present at any meeting, personally or by proxy, that of the said persons so present whose name stands first on the register in respect of such share, shall alone be entitled to vote in respect thereof."

The Income-tax Appellate Tribunal held that the company was a director-controlled company within the meaning of Section 2 (21) (a) of the Excess Profits Tax Act. On an application of the Commissioner under Section 66 (1) the Tribunal referred the following question for the decision of the High Court :—

" Whether in the circumstances of the case and in view of the fact that the twenty shares were held jointly by Nanji Kalidas, a director of the company, with four other persons, it has been rightly held that the appellant company is a director-controlled company within the meaning of Section 2 (21) (a) of the Excess Profits Tax Act ? "

M. C. Setalvad, for the Commissioner.

Sir J. B. Kanga, for the assessees.

JUDGMENT.

KANIA, J.—This reference deals with two applications made by the Commissioner of Income-tax in respect of the assessment of the assessees for two accounting periods, *viz.*, 1st September 1939 to 31st December 1939 and the calendar year 1940. The relevant facts are these: The assessee company is a joint stock company with a share capital divided into 100 shares of Rs. 5,000 each. 43 shares are held by the directors admittedly in their own right and in their individual names. 20 shares stand in the names of Mr. Nanji Kalidas, Mrs. Nanji, Sardar Tribhowandas Jagjivandas, Raja Pandit Anandpuriyaji and Rajya Ratna H. M. Wadia. It is stated in the reference that these shares are held by Nanji Kalidas not in his individual capacity but "as a trustee."

On behalf of the Commissioner it is contended that as these 20 shares are held by five persons in their capacity as trustees it is improper to construe that they have an interest in these shares within the meaning of Section 2 (21) (a) read with clause (c) and the last proviso to that sub-section of the Excess Profits Tax Act. It was argued that the interest there contemplated must be beneficial interest and not merely the interest of a trustee. Before the Tribunal the parties referred to *B. W. Noble Ltd.* v. *Commissioners of Inland Revenue*[1], and *British American Tobacco Co.* v. *Inland Revenue Commissioners*[2]. The Tribunal rejected the contention of the Commissioner and held that it was not necessary that the interest should be beneficial interest. From the application made by the Commissioner for a reference it appears that the decision of Mr. Justice Macnaghten in *J. Bibby and Co.* v. *Commissioners of Inland Revenue*, which was briefly reported in one of the Taxation magazine reports was noticed. That is now reported in (1943) 2 All E. R. 419. It was there held that the interest contemplated by the corresponding section of the English Act must be beneficial interest. That matter went in appeal and in All England Law Reports (1944) Vol. I, page 548, Lord Greene, M. R., in delivering the judgment of the Court of Appeal reversed the decision of the lower Court, and held that except in the case of a bare trustee, perhaps, the question of the holder having a beneficial interest did not arise. It was held that the trustee's interest was sufficient to bring the case within the meaning of that sub-section.* That sets at rest the first part of the argument of the Commissioner.

(1) (1926) 12 Tax Cas. 911.

(2) (1942) 10 I.T.R. Suppl. 67. This reference relates to the decision of the Court of Appeal. It was affirmed by the House of Lords: see [1943] 11 I.T.R. Suppl. 29—Ed.

* The decision of the Court of Appeal was subsequently affirmed by the House of Lords; see [1946] 14 I.T.R. Suppl. 7—Ed.

It was next contended that when there are more than one trustee the management has to be according to the vote of the majority. From that it was argued that if the five trustees at a meeting decided that the voting should be in a particular way, Nanji Kalidas, the director, will not have an authority to vote otherwise, and therefore it cannot be considered that he had a controlling interest in respect of the 20 shares. Before considering this argument it is first necessary to look at the provisions of the trust deed. Mr. Setalvad was given the trust deed and after perusing the same he frankly conceded that under its provisions Nanji had an overriding power to decide questions in the management of the trust and it was further provided in the deed that the trustees must act as directed by Nanji. In view of these provisions in the trust deed the contention that the vote of the majority must prevail must fail. It must be left to the sole discretion of Nanji to vote as he directed. Under the articles of association of the company it is also provided that if Nanji was present at a meeting, as between the company and the shareholders, he had a right to vote as he pleased. Under the circumstances there is no doubt that in the case of the respondents the controlling interest within the meaning of Section 2 (21) (a) of the Excess Profits Tax Act is in the directors. The question submitted to us is:

"Whether in the circumstances of the case and in view of the fact that the twenty shares were held jointly by Nanji Kalidas, a director of the company, with four other persons, it has been rightly held that the appellant company is a director-controlled company within the meaning of Section 2 (21) (a) of the Excess Profits Tax Act?"

Having regard to what is stated above, the answer to the question is in the affirmative. The Commissioner to pay the costs of the reference.

Reference answered in the affirmative.

[IN THE CHIEF COURT OF SIND.]

COMMISSIONER OF INCOME-TAX, BOMBAY, SIND AND BALUCHISTAN

v.

INDIAN LIFE ASSURANCE CO., LTD.

DAVIS, C. J., and THADANI, J. March 12, 1945.

INCOME-TAX RULES, 1922 (BEFORE AMENDMENT IN 1939)*, R. 30—LIFE ASSURANCE COMPANY—DEPRECIATION OF OR LOSS ON SECURITIES—RESERVE FUND—AMOUNTS CARRIED TO RESERVE FUND TO MEET DEPRECIATION OR LOSS APPREHENDED IN FUTURE—WHETHER ALLOWABLE AS EXPENDITURE.

Under rule 30 of the Income-tax Rules the depreciation of or loss on securities or other assets to meet which a reserve fund may be formed must

* For the law after 1939 see cl. (b) of rule 3 of the Schedule to the Income-tax Act as amended in 1939—Ed.

be a depreciation or loss actually suffered and not a depreciation or loss which is apprehended in the future. The amounts carried to the reserve fund must be amounts equivalent to the amounts which could be written off as depreciation of or loss on securities.

Case referred to:

Commissioner of Income-tax, Bombay *v.* Western India Life Assurance Co., Ltd. [1938] (6 I.T.R. 44; A.I.R. 1938 Bom. 345; 176 I.C. 970).

Reference under Section 66 (2) of the Indian Income-tax Act (XI of 1922) by the Commissioner of Income-tax, Bombay, Sind and British Baluchistan: Income-tax Reference No. 50 of 1943.

STATEMENT OF CASE.

"Reference made under Section 66 (2) of the Indian Income-tax Act, XI of 1922 (hereinafter referred to as 'the Act'), in respect of the assessment of the Indian Life Assurance Co., Ltd., of Karachi (hereinafter referred to as 'the Company') for the assessment year 1938-39.

Facts of the Case.—Under rule 25 of the Indian Income-tax Rules as it stood at the time of this assessment life assurance companies whose profits are periodically ascertained by actuarial valuation were assessable on the basis of the average annual net profits disclosed by the last preceding valuation. In the case of the present company an actuarial valuation was made for the period of five years ending on the 31st of May 1937, and the assessment for 1938-39 is the first assessment made on the basis of that valuation.

2. During the five years in question the company maintained a special account which was called the 'investment reserve fund.' Adjustments were made in this account at the end of each year on the basis of the valuation placed by the company on its holding of securities. The history of the account may be briefly summarised as follows:—

Year ending 31-5-33: During this year the actual appreciation in the market value of the securities was Rs. 13,05,492, but a sum of Rs. 4,32,675 was utilised to meet the actual depreciation which had occurred during the previous quinquennium. The balance of Rs. 8,72,817 was taken to the investment reserve fund.

Year ending 31-5-34: The actual appreciation during this year was Rs. 6,52,322. This also was taken to the investment reserve fund, increasing the balance in the fund to Rs. 15,25,139.

Year ending 31-5-35: There was an actual appreciation of Rs. 2,58,202 in the market value of the securities, but the company did not credit this appreciation to the fund as in the two previous years. It ignored the actual appreciation and wrote down the securities to their face value which was found to be Rs. 7,86,044 lower than the actual market value ascertained at the end of the preceding year. This sum of Rs. 7,86,044

was debited to the investment reserve fund, reducing the balance in the fund to Rs. 7,39,095.

Years ending on 31-5-36 and *31-5-37* : In the first of these years there was an appreciation of Rs. 5,30,563 in the market value of the securities and in the second year there was a depreciation of Rs. 2,65,409 leaving a net appreciation of Rs. 2,65,154. As in the year ending on the 31st of May 1935 the company ignored these changes in the market value, but it charged to the investment reserve fund certain small losses amounting to Rs. 11,522 which were incurred on securities sold or redeemed during the two years. Thus the balance remaining in the fund at the end of the five year period was Rs. 7,27,573.

3. When scrutinising the accounts in connection with the assessment for 1938-39 the Income-tax Officer noticed the balance of Rs. 7,27,573 in the investment reserve fund and decided that it should be added to the profits shown by the actuarial valuation under rule 30 of the Income-tax Rules. This rule reads as follows :—

"30. Any amount either written off in the accounts or through the Actuarial Valuation Balance Sheet to meet depreciation of, or loss on, securities or other assets, or which is carried to a reserve fund formed for that sole purpose and not used for any other purpose, may be treated as expenditure incurred solely for the purpose of earning the profits of the business. Any sums taken credit for in the accounts or Actuarial Valuation Balance Sheet on account of appreciation of or gains on the securities or other assets shall be deemed to be income chargeable to tax subject always to deduction of such portion thereof as has been otherwise taken into account in calculating the income, profits or gains."

In accordance with his decision the Income-tax Officer included in the assessment a sum of Rs. 1,45,514, being one-fifth of the balance in the investment reserve fund, and he completed the assessment on a total income of Rs. 5,29,790. A copy of his assessment order is annexed as exhibit A.

4. Being dissatisfied with the Income-tax Officer's decision on this and other points the company appealed to the Appellate Assistant Commissioner of Income-tax, Sind and Baluchistan. The Appellate Assistant Commissioner however held that the company was not entitled to any reduction and he confirmed the assessment made by the Income-tax Officer. A copy of the appellate order is annexed as exhibit B.

5. The company then filed an application to the Commissioner of Income-tax, Bombay, under Sections 33 and 66 (2) of the Act in which the Commissioner was requested either to revise the assessment or to make a reference to the Chief Court. A copy of the application is annexed as exhibit C. Apart from the question relating to the investment reserve fund the company claimed in its application that the Income-tax Officer had not

made the proper allowance in respect of interest on tax free securities. This question however has since been considered by the Chief Court in connection with the company's assessment for 1937-38, and in accordance with the Chief Court's order dated the 19th of September 1940 I have accepted the company's contention for this year also in exercise of my powers under Section 33. Hence there is now only one question at issue.

5. **Question for decision.**—Since I am unable to accept the company's contentions with regard to the investment reserve fund I refer the following question for the decision of the Chief Court :—

"Whether under the provisions of rule 30 of the Income-tax Rules the Income-tax Officer was justified in adding to the profits disclosed by the actuarial valuation a sum of Rs. 1,45,514, being one-fifth of the balance shown in the investment reserve fund."

6. **Opinion of the Commissioner.**—The company claims in the first place that the amount in question is not taxable because it represents a sum which was carried to a reserve formed for the sole purpose of meeting depreciation of or loss on securities and is therefore covered by the first part of rule 30. In this connection I venture to invite a reference to the decision of the Bombay High Court on the case of *Western India Life Assurance Co., Ltd., In re*[1]. In that case it was held that rule 30 "confers an option upon the assessee to write off in his accounts to meet depreciation or to carry to a reserve fund to meet depreciation any amount which is justified by an actual loss in any particular year." The Hon'ble the Chief Justice however made it clear in his judgment that in his view the reserve must be in respect of depreciation or loss which has actually been incurred, and that a reserve established merely to meet possible future losses would not come within the scope of the rule. In the present case there was in fact no loss but a substantial net appreciation in the value of the securities during the five year period. Following the Bombay decision therefore I respectfully submit that the condition prescribed by the first part of rule 30 is not satisfied.

7. The company further claims that the second part of rule 30, under which the Income-tax Officer has included the disputed sum in the assessment, "refers to sums which have been carried to the life assurance fund or to any account other than a specific fund for meeting depreciation of or loss on securities or other assets" (exhibit C) and that since the sum of Rs. 7,27,573 was not carried to the life insurance fund or to any fund other than the investment reserve fund it is not covered by that part of the rule. I can find no warrant for restricting the meaning of the word "accounts" in the manner suggested by the company. In the absence of any indication to the contrary the word "accounts" should, in my opinion, be given its ordinary meaning and should be interpreted as including any account in

(1) [1938] 6 I.T.R. 44.

the balance sheet. I submit therefore that the investment reserve fund is an account for the purpose of rule 30 and that the Income-tax Officer was justified in holding that the sums credited to that account in respect of appreciation in the value of securities are taxable under the rules. As has been shown in paragraph 2 above sums amounting to Rs. 15,25,139 were actually credited to this account in the first two years of the period, and if the view expressed in the preceding paragraph is correct the company was not in fact entitled to deduct from this amount, for income-tax purposes, the sum of Rs. 7,86,044 which was debited to the fund in the third year, since that sum did not represent an actual depreciation in the value of the securities. The actual appreciation in the three later years of the period cannot be taken into consideration since the company did not take credit for it but the only items which in my view the company could legitimately claim to set off against the credits of the first two years are the debits amounting to Rs. 11,522 in respect of losses on securities sold or redeemed. Thus the amount which should have been considered in the assessment was not Rs. 7,27,573 but Rs. 15,25,139—Rs. 11,522=Rs. 15,13,617. The Income-tax Officer has since made a supplementary assessment on this basis.

8. For the above reasons I am respectfully of opinion that the answer to the question which has been stated should be in the affirmative, and that the Income-tax Officer should in fact have added a larger sum, namely one-fifth of Rs. 15,13,617."

Partabrai D. Punwani, for the Commissioner.

F. J. Coltman, for the assessees.

JUDGMENT.

DAVIS, C. J.—This is a reference by the Commissioner of Income-tax, Bombay, Sind and Baluchistan, under Section 66 (2) of the Income-tax Act in which the learned Commissioner referred to this Court for its decision the following question :—

"Whether under the provisions of rule 30 of the Income-tax Rules the Income-tax Officer was justified in adding to the profits disclosed by the actuarial valuation a sum of Rs. 1,45,514, being one-fifth of the balance shown in the investment reserve fund ?"

The matter in dispute appears to lie within a very small compass and that is whether, when under rule 30 of the Income-tax Rules, reference is made to the depreciation of or loss on securities or other assets to meet which a reserve fund may be formed, the depreciation or loss must be a depreciation or loss actually suffered or may be a depreciation or loss which is apprehended in the future. Mr. Coltman for the assessee company contends that rule 30 of the Income-tax Rules is intended to cover provision made under the reserve fund to meet apprehended depreciation or loss, while the learned

advocate for the Commissioner of Income-tax contends that the depreciation or loss for which provision can be made must be depreciation or loss actually suffered and for this purpose he refers to a case of the Bombay High Court reported in *Western India Life Assurance Co., Ltd., In re*[1].

The facts of this case are that in the year 1933 there was an actual appreciation in the market value of securities held by the assessee company of Rs. 13,05,492, out of which a sum of Rs. 4,32,675 was utilized to meet actual depreciation which had occurred during the previous quinquennium, leaving in the investment reserve fund a balance of Rs. 8,72,817. During the year ending 31st May 1934, there was an actual appreciation of Rs. 6,52,322. This was also placed in the investment reserve fund, the balance of which was now increased to Rs. 15,25,139. During the year ending 31st May 1935 there was an actual appreciation of Rs. 2,58,202 in the market value of the securities; but the assessee company did not place this amount to the credit of the investment reserve fund, nor indeed, did the company show this appreciation as assets which might become chargeable to income-tax under Part II of rule 30 of the Income-tax Rules. The assessee company ignored this appreciation and wrote down the securities at their face value by a sum of Rs. 7,86,044. This sum was then debited to the investment reserve fund, reducing the balance to Rs. 7,39,095. During the year ending 31st May 1936 and the year ending 31st May 1937, there was in the first of these two years an appreciation of Rs. 5,30,563 in the market value of the securities and in the second year there was a depreciation of Rs. 2,65,409, leaving a net appreciation of Rs. 2,65,154; as in the year ending 31st May 1935 the company ignored these changes in the market value. They, however, charged certain small losses actually incurred on securities sold or redeemed to the investment reserve fund. This was a sum amounting to Rs. 11,522.

At the end of the five year period then there was, as a result of this accounting in the investment reserve fund, a balance of Rs. 7,27,573. The Income-tax Officer scrutinizing the accounts for the assessment year 1938-39 observed this balance of Rs. 7,27,573 and decided that it should be added to the profits shown in the actuarial valuation under rule 30 of the Income-tax Rules. This rule provides as under :—

"Any amount either written off in the accounts or through the Actuarial Valuation Balance Sheet to meet depreciation of, or loss on, securities or other assets, or which is carried to a reserve fund formed for that sole purpose and not used for any other purpose, may be treated as expenditure incurred solely for the purpose of earning the profits of the business. Any sums taken credit for in the accounts or Actuarial Valuation Balance Sheet on account of appreciation of or gains on the securities or other assets shall

(1) [1938] 6 I.T.R. 44.

be deemed to be income chargeable to tax, subject always to deduction of such portion thereof as has been otherwise taken into account in calculating the income, profits or gains."

The Income-tax Officer accordingly included in the assessment for the year 1938-39 one-fifth of this amount, Rs. 7,27,573, *i.e.*, Rs. 1,45,514. The Income-tax Officer completed the assessment on a total income of Rs. 5,29,790.

Now, if the assessee company can bring this sum of Rs. 7,27,573 within the provisions of rule 30 of the Income-tax Rules as a reserve fund properly formed under the provisions of that rule for the sole purpose of meeting depreciation of or loss on securities, it will be entitled to treat this sum as expenditure incurred solely for the purpose of earning the profits of the business, and therefore to be excluded for the purpose of the assessee's liability to income-tax.

Mr. Coltman argues that clearly the purpose of the reserve fund is to meet not only present events but also future contingencies. According to the provisions of rule 30 of the Income-tax Rules, he argues, it is contemplated that amounts carried to a reserve fund are to be exempt from income-tax for so long as they serve their useful purpose. If any sum should, for instance, be brought out of the reserve fund and credited and used for any other purpose in the accounts, then this sum becomes liable to income-tax; it would, he argues, be frustrating the purpose of the rule if it were permitted to carry to the reserve fund only such sums as are necessary to meet depreciation or loss actually suffered and to make no provision for the future.

Mr. Coltman points out, the real point in issue in the Bombay case cited was the question as to whether it was the assessee or the Income-tax Officer who was permitted to treat as expenditure incurred solely for the purpose of earning profits of the business sums carried to the reserve fund and that the remarks of the learned Chief Justice to the effect that there can be carried properly to the reserve fund only such sums as are sufficient to meet the depreciation or loss actually suffered, were obiter; indeed, if sums carried to the reserve fund were to be set off only against the depreciation or loss actually incurred, then taking the period of three years as a separate entity—and it must be so taken—the Bombay High Court should have set off against the depreciation in the first two years the appreciation accruing in the third year and have struck a credit balance: this the learned Judges did not do, holding that once sums have been properly carried to the reserve fund to meet depreciation or loss of the first two years, they were not affected by subsequent appreciation of the securities in the third year, which might turn the loss in the first two years into a gain. These are Mr. Coltman's arguments.

I do not think, however, that this question can be decided on the *obiter dicta* of the learned Judges, but it must, I think, be decided on the actual words used in rule 30. Rule 30, it is conceded, must be read with rule 25. Rule 25 refers to the periodical ascertainment of profits and refers to the average annual net profits disclosed by the last preceding valuation. But the fact that the profits or gains of a life assurance company are to be estimated on the basis of a three year or five year period as one entity, does not, I think, affect the answer to the question, whether the reserve fund is to meet actual or apprehended depreciation or loss. The answer to this question depends, I think, on the words of rule 30 itself. It is true that it is desirable for the assurance company to have funds in reserve; it is also desirable for other companies to have funds in reserve, but it does not follow that sums placed in reserve are to be exempted from income-tax, even before they are so placed. While it may be argued that the very purpose and nature of a reserve fund is to meet future contingencies, liabilities to be incurred as well as those incurred, and while it is to be borne in mind that a fiscal statute must be construed strictly and in favour of the subject, nevertheless, it appears that rule 30 makes special provision whereby certain amounts otherwise liable to taxation may be exempted from this liability, but only on the basis of expenditure incurred solely for the purpose of earning the profits of the business. When these amounts are to be so treated, it appears to me, it follows that what is properly to be carried to the reserve fund for the purpose of rule 30 is not any amount that the directors in their discretion think necessary to safeguard the future position of the company, or to meet future contingencies, but only such amounts as are necessary to meet depreciation or loss that has actually occurred or has actually been suffered. It could not, for instance, be argued that the amounts written off, which is the first matter dealt with in the rule, can be any amounts other than those which arise from actual loss or actual depreciation on securities. When, therefore, an alternative to writing off is offered in the form of a reserve fund, it follows that the amounts carried to this reserve fund formed for the same sole purpose can equal only those which might have been written off. The amounts carried to the reserve fund must be amounts equivalent to the amounts which could be written off as depreciation of or loss on securities. It is not, therefore, open to the assessee company to write off amounts larger than those actually lost by depreciation of securities. It is true that under new rule 2, sub-rule (3), the Income-tax Officer after consultation with the Superintendent of Insurance has been given discretion to control to some extent amounts which can be regarded as fair provision for meeting contingencies and should be free from income-tax, but this does not, in my opinion, affect the answer to the question now before us. I think, therefore, that the answer to the question must be in the affirmative.

THADANI, J.—I concur, and would add only a few words. Rule 30 of the Income-tax Rules enables an assessee company to deal with the depreciation of or loss on securities in one of the two following ways: (1) by writing off an amount which must necessarily mean an ascertained amount in the accounts or through the actuarial valuation balance-sheet, or (2) by carrying an amount to a reserve fund formed for that sole purpose and not for any other purpose. In whichever way the assessee deals with the depreciation of or loss on securities, it is to be treated as expenditure incurred solely for the purpose of earning the profits of the business.

I think the words "treated as expenditure incurred solely for the purpose of earning the profits of the business" in rule 30 provide a clue as to the extent to which a reserve fund can be formed for the purpose of meeting the depreciation of or loss on securities. Under Section 10 of the Income-tax Act, "the tax shall be payable by an assessee under the head business in respect of the profits or gains of any business carried on by him." Such profits or gains, however, shall be computed after making certain allowances mentioned in sub-section (2) of Section 10. Clause (xii) of sub-section (2) of Section 10 refers to "any expenditure (not being in the nature of capital expenditure) incurred solely for the purpose of earning such profits or gains." It is not contended and it is not possible to contend that the expenditure referred to in clause (xii) means anything more than actual expenditure. When, therefore, rule 30 of the Income-tax Rules treats the reserve fund mentioned in that rule as expenditure, the word "expenditure" in rule 30 must have the same meaning as in clause (xii) of sub-section (2) of Section 10 of the Income-tax Act.

Mr. Coltman has relied upon the schedule containing clause (b) of rule 3 of the rules framed for the computation of the profits and gains of an insurance business. The original schedule was repealed by the Repealing Act, 1927 (XII of 1927), and this schedule was added by Section 84 of the Income-tax (Amendment) Act, 1939 (VII of 1939). Clause (b) of rule 3 in the new schedule added by Section 84 of the Income-tax (Amendment) Act of 1939 was made after the assessment period in question. Moreover, I do not think that clause (b) of rule 3 necessarily suggests that an assessee company is at liberty to set apart any sums in the discretion of the directors in the reserve fund formed for the sole purpose of making provision for depreciation or loss in the market value of the securities. Clause (b) in no way suggests or attempts to suggest that the word "expenditure" in rule 30 is not to be read with the word "expenditure" used in clause (xii) of sub-section (2) of Section 10 of the Income-tax Act. It appears to me that when clause (b) of rule 3 in the new schedule is read with the proviso to clause (b), the idea was to empower the Income-tax Officer to make adjustments in the matter of the valuation of the securities and the extent of the

reserve fund formed solely for the purpose of depreciation of or loss on the market value of the securities, a power which had been denied to the Income-tax Officer by the Bombay High Court in *Western India Life Assurance Co., Ltd., In re* [1]. It does not in any way affect the interpretation of rule 30 of the Income-tax Rules, which we have put on it.

Reference answered in the affirmative.

[IN THE OUDH CHIEF COURT.]

NAWAB NAWAZISH ALI KHAN

v.

COMMISSIONER OF INCOME-TAX, C. P. AND U. P.

BENNETT and MADELEY, JJ.

September 29, 1944.

INDIAN INCOME-TAX ACT (XI OF 1922), SECS. 2 (1) (a) & (c); 4 (3) (viii) & 66—INCOME FROM SALE OF FOREST TREES—WHETHER AGRICULTURAL INCOME—JURISDICTION OF HIGH COURT—QUESTION NOT REFERRED —WHETHER CAN BE CONSIDERED—RESIDENTIAL BUILDING—WHETHER IN THE IMMEDIATE VICINITY OF LAND—WHETHER ENTITLED TO EXEMPTION.

Income from the sale of forest trees growing on land naturally and without the intervention of human agency, even if the land is assessed to land revenue, is not agricultural income within the meaning of Section 2 (1) (a) of the Income-tax Act and is not exempt from income-tax under Section 4 (3) (viii) of the Act.

It is not open to an assessee to travel outside the scope of the question referred under Section 66 (1) of the Act.

The assessee sought to claim exemption under Section 2 (1) (c) of the Act in respect of the rental value of his residential house. The Tribunal held that since the building was at a distance of sixteen miles from the land, it could not be deemed to be in the immediate vicinity of the land to attract the proviso to Section 2 (1) (c):

Held, *that there was no reason to take a view different from that taken by the Tribunal and that the assessee was not entitled to the benefit of Section 2 (1) (c).*

Maharaja of Kapurthala v. *Commissioner of Income-tax, C. P. and U. P.* [*1945*] (*13 I.T.R. 74*) and *Special Manager, Court of Wards, Majgawan Estate* v. *Commissioner of Income-tax, U.P. and C.P.* [*1945*] (*13 I.T.R. 94*) followed.

References under Section 66 (1) of the Indian Income-tax Act (XI of 1922) by the Income-tax Appellate Tribunal: Civil References Nos. 5, 7 and 8 of 1942.

(1) [1938] 6 I.T.R. 44.

STATEMENT OF CASE.

(Civil Reference No. 7 of 1942).

" This is an application under Section 66 (1), Income-tax Act, by the assessee to refer to the Court three questions of law which are said to arise from the order of this Bench, dated 2nd December 1941, in R. A. A. No. 15 (U. P.) of 1941-42.

2. The assessee owns an estate in Pargana Charda in the district of Bahraich. By his assessment order, dated 4th March 1939, the Income-tax Officer, Gonda, determined under Section 23 (3) a sum of Rs. 38,000 as having been realised by the assessee in the accounting year for the assessment under reference by sale of timber of forest trees in his estate and the said sum was included in the assessable income. On appeal it was urged before the Appellate Assistant Commissioner that since the forest land was assessed to land revenue, the revenue derived from such land amounted to agricultural income within the meaning of Section 2 (1) (a) and was as such exempt from income-tax by reason of the exemption provided under clause (viii) of Section 4 (3). Both the Income-tax Officer and the Appellate Assistant Commissioner, after examining this contention elaborately, reached the conclusion that the forest land was not assessed to land revenue. In the course of the hearing of the appeal before the Appellate Assistant Commissioner, however, an alternative contention appears to have been advanced to the effect that it was a case of the conversion of capital from one form to another and that as such the sums realised were of a capital nature. This plea was also negatived and the appeal was rejected. Thereupon an appeal was preferred before this Tribunal amplifying the two grounds already taken and pleading further that this item of income represented a casual receipt, thereby seeking to invoke the aid of the exemption embodied in clause (vii) of Section 4 (3). Besides this question objection was taken to the assessment with reference to another item, *viz.*, the rental value of the assessee's residential house in Bahraich, with reference to which exemption was sought under the proviso to Section 2 (1) (c). This claim was disallowed both by the Income-tax Officer and the Appellate Assistant Commissioner on the ground that the building in question was not, as contemplated in the proviso, " on or in the immediate vicinity of the land." The appeal made to this Tribunal was also dismissed on all the points and the assessee has now applied that the case should be stated to the Court and has claimed that the following questions of law arise out of the order of this Bench :—

(a) Whether the receipts from sale of forest is agricultural income under Section 4 (3) (viii) of the Income-tax Act ;

(b) Whether in the event of the sale of the whole of a forest, receipts from such sale is not of a casual and non-recurring nature and thus

exempt from the imposition of income-tax under Section 4 (3) (vii) of the Income-tax Act; and

(e) Is not a residential house of a landed proprietor exempt from taxation merely because it is situated at a distance of 15 miles from his estate.

3. The Commissioner of Income-tax, Central and United Provinces, Lucknow, has under rule 54 of the Appellate Tribunal Rules, filed a reply to the reference application objecting to the reference of any of the questions proposed. With regard to the first question, however, he points out that the counsel for the assessee conceded that the receipt in question was not agricultural income but if notwithstanding the same the point is held to arise out of the order of the Tribunal, the question may be referred in the revised form proposed by him.

4. Before dealing with the questions adumbrated in the assessee's application it is necessary to point out that the Tribunal heard the three appeals filed by the assessee in respect of the years 1937-38, 1938-39 and 1939-40 together and while it set out the detailed reasons for its conclusions in its order passed on the appeal relating to the assessment year 1937-38, it contented itself in its orders relating to the two subsequent years with a mere reference to the earlier order and proceeded to record its findings without repeating the grounds of the decision.

5. It has also to be mentioned incidentally that even though the original assessment, which is the subject-matter of the appeal out of which this reference has arisen, was based on a computation of Rs. 38,000 as the sum realised by the sale of timber trees in the relevant accounting year, it was subsequently discovered by the Income-tax Officer that a larger amount was in actual fact realised and consequently proceedings were instituted under Section 34 and on 29th September 1941, a sum of Rs. 72,068 was determined to be the sale proceeds realised. This fact, however, has no bearing upon the present proceedings as both the appeals before the Appellate Assistant Commissioner and the Tribunal were against the original assessment order and the enhancement itself was effected after the institution of appeal before the Tribunal.

6. There is no doubt that a question of law arises from the order of the Tribunal as to whether the income derived from the sale of wood from forests can be said to be derived from land used for agricultural purposes or from agriculture. Under clause (viii) of Section 4 (3) agricultural income is not to be included in the total income of an assessee and the expression 'agricultural income' has been defined in the Act itself as meaning 'any rent or revenue derived from land which is used for agricultural purposes and is either assessed to land revenue in British India or subject to a local rate assessed and collected by officers of the Crown as such.' The Income-

tax Officer went elaborately into the question of the assessment of the forests to land revenue and came to the conclusion, with reference to the settlement records and other *indicia*, that the income from the timber trees was never included in the assessable assets and was not assessed to land revenue.

7. This finding was not, however, examined by the Bench in view of an admission made by Khwaja Feroz-ud-Din Ahmad, counsel for the appellant, at the time of the hearing of the appeal (an admission which has been placed on record) that, in view of the decisions in *Province of Bihar* v. *Maharaja Pratap Udai Nath*[1], *Chandrasekhara Swamigal* v. *Duraiswami Naidu*[2] and *Kesho Prasad Singh* v. *Sheo Pragash Ojha*[3], he did not contend that land overgrown with spontaneous forests can be said to be used for purposes of agriculture. He further admitted that the forest which has been cut was spontaneous growth and existed at the time the estate was granted to the forefathers of the appellant and nothing was ever done to the land to make it fit for forestry. While the former admission, being on a question of law, may not be said to be binding, the latter as an admission of fact, is, in our opinion, definitely binding on the assessee.

8. Having regard to the definition of agricultural income in the Act, even if the land on which the forest has grown is assessed to land revenue, it is necessary to establish that the land was used for agricultural purposes before exemption under clause (viii) can be claimed. A land cannot be said to be used for agricultural purposes where what is grown on it is a forest, as forestry or sylviculture is not included in the term "agriculture"; agriculture implies cultivation of the soil and where nothing is done to the soil to prepare it for the purpose of forest growing and the forest is a spontaneous growth, the land cannot be said to be used for agricultural purposes. As pointed out in the case of the Province of Bihar above referred to, the trees cannot be said to have grown as the result of cultivation; in fact it was the absence of cultivation that permitted the area to develop into a jungle. These conclusions, to our minds, necessarily follow from the admissions of fact made by the assessee's counsel and we are of the opinion that from those findings the following question of law arises :—

"Whether income from the sale of forest trees growing on land naturally and without the intervention of human agency, even if the land is assessed to land revenue, is agricultural income within the meaning of Section 2 (1) (a) of the Income-tax Act and as such exempt from income-tax under Section 4 (3) (viii) of the Act."

9. The point involved in the second question was not raised either before the Income-tax Officer or before the Appellate Assistant Commissioner and, although it is admittedly a question of fact, no evidence was led on the point. The premises assumed in the question are that the whole of the

(1) [1941] 9 I.T.R. 313. (2) (1931) I.L.R. 54 Mad. 900.
(3) (1923) I.L.R. 44 All. 19 confirmed by the Privy Council on appeal in I.L.R. 46 All. 831.

forest was in one transaction sold away with a view to bringing the land under cultivation and that after the forest was denuded, the land was let out to tenants for cultivation. Discarding that plea altogether, this Bench found as a matter of fact that for several years past the assessee and his predecessors were deriving regular income from the sale of trees and that saplings in the important forest tracts were being preserved with a view to future profits. It is therefore clear that the question whether the receipts were of a casual and non-recurring nature is altogether one of fact and in view of our finding thereon, no question of law arises therefrom for reference. Khwaja Feroz-ud-Din Ahmad, who appeared to argue this reference, agreed with this view before us. The second question that is propounded in the reference application does not therefore arise.

10. The further question as to whether the net receipts from the sale of forest trees were assessable income liable to income-tax or merely capital converted into cash and as such not assessable, raised in the appeal before the Tribunal (though not at the earlier stages), has not, however, been propounded in the reference application, nor was it urged by the assessee's counsel at the time of the hearing of this application.

11. Turning to the third question, it was held by the Tribunal that since the building which is claimed to have been used for residential purposes by the assessee is admittedly at a distance of 16 miles from the land, it cannot be deemed to be in the immediate vicinity of the land to attract the proviso to Section 2 (1) (c). Since the matter turns upon the interpretation of the expression "immediate vicinity" used in the statute, we regard it as giving rise to a question of law.

12. Under Section 66 (1) of the Income-tax Act, the following questions are therefore referred to the Chief Court of Oudh at Lucknow :—

(1) Whether income from the sale of forest trees growing on land naturally and without the intervention of human agency, even if the land is assessed to land revenue, is agricultural income within the meaning of Section 2 (1) (a) of the Income-tax Act and as such exempt from income-tax under Section 4 (3) (viii) of the Act.

(2) Whether in view of the admitted distance of the residential building from the land, the assessee is entitled to the benefit of the proviso to Section 2 (1) (c)."

Akhlaque Husain, for the assessee.

S. C. Dass, for the Commissioner.

JUDGMENT.

These are references by the Income-tax Appellate Tribunal under Section 66 (1) of the Indian Income-tax Act. One question referred is common to all the three references, namely :—

Whether income from the sale of forest trees growing on land naturally and without the intervention of human agency, even if the land is assessed to land revenue, is agricultural income within the meaning of Section 2 (1) (a) of the Income-tax Act and as such exempt from income-tax under Section 4 (3) (viii) of the Act.

In References Nos. 5 and 8 of 1942, this is the only question referred. In Reference No. 7 of 1942 there is a second question namely,

Whether in view of the admitted distance of the residential building from the land, the assessee is entitled to the benefit of the proviso to Section 2 (1) (c).

The assessee, Nawab Nawazish Ali Khan, owns an estate in the district of Bahraich. The assessment years under consideration are 1937-38, 1938-39 and 1939-40. The assessee realised sums of Rs. 49,481, Rs. 38,000 and Rs. 14,550 in the relevant years respectively from the sale of timber of forest trees, and these sums were included in his income for the purpose of income-tax.

The assessee's learned counsel also raised the question whether receipts from such sales constitute income and not capital. The reference order in each case shows that this question was raised in the appeal before the Tribunal (though not before), but it was not propounded in the reference application, nor was it urged by the assessee's counsel at the hearing of the application by the Tribunal.

We have considered in other cases (Civil References Nos. 9 of 1942 and 2 of 1944)* whether in similar circumstances it is open to an assessee to travel outside the scope of the question referred, and for the reasons given by us in our judgment on those references we held that he cannot. We are not therefore prepared to allow the assessee to raise this question now.

The general question which is common to all three references was considered by us at length in Civil Reference No. 1 of 1942†, where we held that such income was not agricultural income within the meaning of Section 2 (1) (a) of the Act. We give the same answer to the question in these cases.

The other question referred in Reference No. 7 of 1942 was not argued before us and we assume that the learned counsel for the assessee felt that he could not contest the decision of the Tribunal that the assessee was not entitled to the benefit referred to. The Tribunal pointed out in its appellate order that " objection to the inclusion of the annual value of the appellant's residential house in Bahraich should have been taken by way of appeal from the original order of assessment dated 7th December 1937, and not in the present appeal which arises out of the order of assessment as revised under Section 34." In their referring order the Tribunal mentions that

* Since reported as *Special Manager, Court of Wards, Majgawan Estate* v. *Commissioner of Income-tax, U.P. and C.P.* [1945] 13 I.T.R. 94.

† Since reported as *Maharaja of Kapurthala* v. *Commissioner of Income-tax, C.P. & U.P.* [1945] 13 I.T.R. 74.

the distance of the building is 16 miles from the land and concludes that it cannot be deemed to be in the immediate vicinity of the land so as to attract the provision invoked. We know nothing further about the facts and can only say that we see no reason to take a view different from that taken by the Tribunal.

We answer the questions propounded in these references accordingly. The assessee will pay the costs of each reference. We fix the fee of the counsel for the Income-tax Department at Rs. 100 in each reference.

References answered accordingly.

[IN THE CALCUTTA HIGH COURT.]

SM. CHARUSILA DASSI AND OTHERS, *In re.*

GENTLE and ORMOND, JJ. January 16, 1946.

INDIAN INCOME-TAX ACT (XI OF 1922), SEC. 4 (3) (i)—CHARITABLE PURPOSES—TRUST FOR CONSTRUCTING TEMPLES AND HOSPITAL FOR FEMALES—WHETHER WHOLLY FOR CHARITABLE PURPOSES—WHETHER INCOME EXEMPT—BURDEN OF PROOF OF EXEMPTION—PUBLIC TEMPLE—CHARACTERISTICS—FEEDING OF POOR OR CONSECRATION CEREMONY—WHETHER CHARITABLE PURPOSE—EFFECT OF ALTERATION OF DEED IN ASSESSMENT YEAR.

A widow, by a deed of settlement, transferred certain properties absolutely and for ever to a body of five trustees including herself and her husband's adopted son on trust for the purpose of constructing twin temples and installing in one of them a deity which she had established in her house and in the other a marble image of her religious preceptor. The deed also provided for the establishment of a hospital for females in memory of the settlor's husband. The temples were in the course of construction. No portion of the income of the trust was applied for the purpose of the hospital and could not, under the terms of the trust, be applied until the temples had been constructed and the deities installed therein. The Commissioner of Income-tax contended that the trust was no more than a private religious trust and that that part of the trust income which would be devoted to the hospital and dispensary would alone be exempt under Section 4 (3) (i) of the Income-tax Act:

Held, *that, on a proper construction of the deed of trust, so much of the income of the trust as was not applied for the purpose of constructing and maintaining the hospital was not exempt from tax under the provisions of Section 4 (3) (i) of the Indian Income-tax Act.*

The trust, which the settlor created with respect to the temple, its erection and all matters and things appertaining to it, was a private trust and was not one for public charitable purposes.

The reference must be decided upon the trust deed and the position which existed during the accounting year and any subsequent alteration by means of a later deed could not affect that position.

The burden was upon the assessees to establish that the income from the trust was exempt from taxation.

The provision in the deed of endowment for the feeding of the poor was incidental to the puja of a deity and that did not make the endowment anything beyond a private one.

The provision for consecration in the deed did not carry the matter any further to show an intention to create a public religious trust. Such a provision was equally appropriate in respect of a temple for a deity whose worship was to be private.

The incident that a trust is irrevocable does not make it a public one.

The prosad utsarga *ceremony dedicates a temple to a deity, it does not consecrate the land upon which the temple is erected.*

The main characteristic of a public temple is that it is intended for the use of the public at large or a specified class, who are entitled to the right of worshipping in it.

The complete divestment, by the author of the trust, of any interest for himself or herself or for members of his or her family in the property over which the trust was created, will not thereby make the trust a public one.

Cases referred to :—

Commissioner of Income-tax, Bihar and Orissa *v.* Maharaja Visweswar Singh [1935] (3 I.T.R. 216 ; I.L.R. 14 Pat. 785 ; 156 I.C. 116 ; A.I.R. 1935 Pat. 342 ; 16 P.L.T. 351 ; 7 R.P. 685).

Gayaprasad *v.* S. S. Bhargo [1934] (A.I.R. 1934 Nag. 48).

Gir Har Saroop *v.* Bhagwan Din [1935] (A.I.R. 1935 Oudh 96).

Gopala Mooppanar *v.* Subramania [1914] (26 I.C. 7).

Manohar Ganesh Tambekar *v.* Lakhmiram Govindram [1887] (I.L.R. 12 Bom. 247 ; 12 Ind. Jur. 387).

Nabi Shirazi *v.* Province of Bengal [1942] (I.L.R. [1942] 1 Cal. 211).

Prosad Das Pal *v.* Jagannath Pal [1932] (37 C.W.N. 181).

Sathappayyar *v.* Periasami [1890] (I.L.R. 14 Mad. 1).

Statement of Case under Section 66 (2) of the Indian Income-tax Act (XI of 1922) by the Commissioner of Income-tax, Bengal: Income-tax Reference No. 1 of 1941.

STATEMENT OF CASE.

" 1. As required by the assessees, Srimati Charusila Dassi and others in their capacity as trustees for the Srimati Charusila Trust Estate, I beg to draw up the following statement of the case and refer to the Hon'ble High Court of Judicature at Fort William in Bengal under Section 66 (2) of the Indian Income-tax Act, XI of 1922, the question of law formulated in paragraph 4 below together with my own opinion thereon. The case was pending before me prior to the coming into force of Part II of the Indian Income-tax (Amendment) Act, 1939, and therefore falls under Section 14 (c)

of the Indian Income-tax (Amendment) Act, 1940, to be referred by me and not by the recently constituted Appellate Tribunal.

2. **Facts of the Case.**—The petitioners were assessed for the assessment year 1939-40 as trustees of 'The Srimati Charusila Trust Estate' on a total income of Rs. 49,691. There is no dispute about the quantum of income and the only point for determination is whether the income of the trust is exempt from tax under the provisions of Section 4 (3) (i) of the Indian Income-tax Act, 1922. Briefly the point for determination is whether the trust is a public or a private religious trust. The facts relating to the trust are as follows:—

On 11th March 1938, Srimati Charusila Dassi, widow of Akhoy Kumar Ghose, by a deed of settlement transferred certain properties absolutely and for ever to a body of five trustees including herself and her son on trust for the purpose of constructing twin temples at Deoghar in Bihar and installing in one of the temples a deity named Iswar Sree Sree 'Sree Gopal' which she had established in her house at Calcutta and in the other a marble image of Sree Sree Iswar Balanand Brahmachari Maharaj who was her 'Guru' or religious preceptor. The deed also provides for the establishment of a hospital for females at Deoghar in memory of the settlor's husband. The hospital however is not to be constructed until the temples have been built.

A copy of the trust deed is appended and marked annexure 'A.'

The following are the principal provisions of the trust deed:—

The settlor (Srimati Charusila Dassi) states that she has established a deity named 'Sree Gopal' in her house and has been regularly performing puja to the said deity. She goes on to say that she has been erecting a twin temple or Jugal Mandir and a Nat Mandir (the latter in memory of her son) at Deoghar and wishes to instal in one of the temples the said deity 'Sree Gopal' and such other deities as she may establish during her lifetime and in the other temple a marble image of her late preceptor or Guru whom she regards as divine. She therefore grants, conveys and transfers certain properties to the trustees to have and to hold for ever upon the following trusts:—

(i) The trust is to be called 'The Srimati Charusila Trust.'

(ii) The income of the trust is to be used for its upkeep etc., and for the completion of the twin temples and Nat Mandir. The settlor is to be allowed to occupy during her lifetime free of rent a certain trust property known as "Charunibas."

(iii) After completion of the temples the deity 'Sree Gopal' and the marble image of the Guru are to be installed there 'in the manner enjoined by the Hindu Sastras.'

(iv) After the construction of the temples certain annual sums are to be spent on the *sheba* and puja of the deities and on certain festivals.

(v) A reserve fund is to be constituted.

(vi) A hospital for Hindu females to be established at Deoghar in memory of the settlor's husband and an outdoor dispensary for out-patients of any religion. The hospital, however, is not to be established until the construction of the temples has been completed.

(vii) The supreme control of the trust properties vests in the board of trustees.

(viii) The settlor reserves the power of removing any of the trustees for misconduct etc., and has the power of filling any vacancy so caused.

(ix) In the case of vacancies by death etc., the vacancy is to be filled by the board of trustees subject to certain conditions.

(x) The sole *shebait* of the deities is the settlor herself during her life and after her death or retirement Sree Mohanand Brahmachari. Provision is made for succession to the *shebaitship* after his death.

(xi) The management of the trust is to be in accordance with certain rules which provide for an annual meeting etc., of trustees. The settlor is to be the first managing trustee.

(xii) The *pronamis* and perquisites to be offered to the deities to form part of the trust estate but the *shebait* is to have no claim on them.

(xiii) If the trustees are not unanimous the view of the majority is to prevail but during the settlor's lifetime her decision is to be final.

The temples are at present still in the course of construction and the deities have not yet been installed. As for the hospital—no portion of the trust's income has yet been applied to this purpose and cannot under the terms of the trust be applied until the temples have been constructed and the deities installed therein.

3. The Income-tax Officer held—for the reasons given in his assessment order, dated the 17th June 1940, a copy of which is attached and marked annexure B—that the trust was a private religious trust which was not exempt from tax under the provisions of Section 4 (3) of the Income-tax Act as its income did not enure for the benefit of the public, at any rate during the lifetime of the settlor.

The petitioners thereupon appealed to the Appellate Assistant Commissioner 'A' Range, Calcutta, who for the reasons given in his order, dated the 10th September 1940, upheld the action of the Income-tax Officer and dismissed the appeal. A copy of the appellate order is appended and marked annexure 'C.'

The petitioners have now requested me to grant relief under Section 33 of the Act or in the alternative to refer to the High Court certain questions of law. A copy of their application is filed and marked annexure 'D.'

4. **Question of law.**—As I do not see my way to grant any relief under Section 33 I refer for your Lordships' decision the following question of

law which appears to me to arise out of the Appellate Assistant Commissioner's order :—

Whether on a proper construction of the deed of trust so much of the income of the trust as is not applied for the purpose of constructing and maintaining the female hospital is exempt from tax under the provisions of Section 4 (3) of the Indian Income-tax Act?

5. **Opinion of the Commissioner.**—So far as the establishment of a female hospital is concerned the Department admits that as soon as monies are applied from the trust income for this purpose such monies will be exempt as the hospital when established will certainly be a charitable institution.

As for the other provisions of the trust it is clear that, except for the reservation in favour of the settlor to reside in the trust premises known as 'Charunibas' (item (3) of the trust deed) and the provision which is implied in item (2) of the deed that rates and other charges for the upkeep and maintenance of 'Charunibas' will have to be met out of the income of the trust estate, the trust is for a religious purpose.

The main question for decision therefore is whether the portion of the trust which relates to the construction of the temples and the installation and worship of the deities is a public or private religious trust. If it is a public religious trust the income will be exempt but if it is a private religious trust the income will be taxable, if in the words of the last line of Section 4 (3) of the Act such income 'does not enure for the benefit of the public.'

In the present case the construction of the temples has not yet been finished and the deities have not been installed. The only way, therefore, of ascertaining whether the trust is a public or private one is from the trust deed itself. In other words what has to be ascertained from the trust deed is whether the temples are intended by the settlor for the use of the public as a right. The deed itself does not even mention the public and gives the public no right whatever. Had the settlor intended to give the public any right she would, in my opinion, have expressed her intention clearly in the deed. On the other hand, the private character of the temples may be inferred from the fact that the idol 'Sree Gopal' for whose benefit one of the temples is being erected is obviously the private deity of the settlor and the public have no right to worship that deity. The other temple is intended for the installation of the image of the settlor's late spiritual guide in whom—so far as I am aware—the general public have no interest. The other building, the 'Nat Mandir' is *in piam memoriam* of the settlor's son and appears to be of no public interest or concern.

I am, therefore, of opinion that, except for the provision for founding a female hospital, the provisions of the trust are entirely a family affair and are inconsistent with the public character of a trust. Furthermore I am

of opinion, that so much of the income of the trust as is not applied for the purpose of constructing and maintaining the female hospital does not enure for the benefit of the public.

The answer to the question formulated should, therefore, in my opinion, be in the negative."

N.C. Chatterji with *K. Basu*, *B. B. Sarkar* and *A.C. Sen*, for the assessees.

S. K. Gupta and *J. C. Pal*, for the Commissioner.

JUDGMENT.

GENTLE, J.—This reference by the Commissioner of Income-tax of Calcutta arises out of a deed of settlement dated 11th March 1938, executed by Sreemati Charusila Dassi (hereinafter called "the settlor") in favour of herself, her deceased husband's adopted son, Debi Prosanna Ghose, and three other gentlemen, who were not members of her or her husband's family (they are hereinafter called "the trustees"). By the deed the settlor created a trust, called the Sreemati Charusila Trust Estate, of lands and other immovable properties in Deoghar, Bihar and in Calcutta (stated to be worth Rs. 10 lacs) which she conveyed unto the trustees to receive the income therefrom, subject to the trusts therein mentioned. The lands and properties comprised :—

(a) a piece of land at Karanibad in Deoghar upon which to build a temple,

(b) a house and land known as "Charunibas" in Deoghar in which the settlor resided,

(c) five immovable properties in Calcutta.

The trusts mentioned in the deed were :—

1. To permit the settlor to use and occupy "Charunibas" free of rent during her lifetime and to effect repairs thereto as reasonably desired by her.

2. Out of the income, in the next place, to complete the construction of the twin temple or Jugal Mandir and the Nat Mandir at Karanibad according to plans and specifications approved by the settlor.

3. After completion of the temple to instal therein the deity "Sree Gopal", which the settlor had established in her house, and a marble image of Sree Sree Iswar Balanand Brahmachari Maharaj, the settlor's *guru* and religious preceptor, in the manner enjoined by the Hindu *Sastras* and to celebrate within the temple land the founding or the consecration ceremony of the temple and the installation ceremony of the deity and the image.

4. To pay for the daily *sheba* and periodic festivals of the deity, or such other deities as might be installed, and of the image, in the manner prescribed in schedule E to the deed.

5. To form a reserve fund out of the income and from donations.

6. To establish and manage a hospital for Hindu females and a dispensary for all patients of any religion or creed whatsoever, to the extent of Rs. 12,000 annually, or such sum as would be available and sufficient after meeting the expenses of the other trusts and after paying the allowances of the *shebait*, trustees, members of the temple committee and the office charges in Calcutta and Deoghar.

The deed directs that the management of the trust should vest in a board of trustees; the trustees, previously mentioned, should form the original board; the settlor reserved the power in her absolute discretion to remove any trustee for the reasons stated in the deed and to fill any vacancy in the board; after her death any vacancy to be filled by the trustees from among the persons or sects therein mentioned; the settlor to be the first *shebait* and after her death or retirement a person therein named to suceed her and thereafter the *shebait* should be the Jugal Mandir *shebait*; the general management, conduct and transaction of business of the trusts and exercise of the functions of the trustees, *shebait*, committee and officers and servants and employees should be in accordance with the rules in schedule A to the deed; the settlor during her lifetime, and the trustees after her death, should be at liberty to add to, make, vary and repeal all or any of such rules as they might think fit in relation to any matter within the scope of their authority; the *pronamis* and perquisites offered to the deities and image should form part of the trust estate and neither the *shebait* nor anyone else should have interest or claim in or over the same; during the lifetime of the settlor her decision at a meeting of the board of trustees should prevail and action taken concerning the administration of the trusts according to her decision.

The rules in schedule A, *inter alia*, provide that the temple committee should consist of the Jugal Mandir *shebait* and 6 pious Hindu residents of Deoghar, appointed by the trustees; subject to the supreme control of the trustees, the temple committee and *shebait* should act in consultation in the matters of detail and daily worship and *bhoga*; the remuneration to be paid to the *shebait* (except the settlor), trustees and the temple committee and the minimum staff (about 33 persons) of the temple, to be as therein specified.

Schedule E to the deed provides for the daily *bhoga* of the deities and image; daily food for 60 persons at noon and for 36 persons at night; the annual festivals to be celebrated, including free distribution of cold drinking water, molasses and grain, at a festival during the month of Baisakh, and free distribution of *bhog* to all present at a festival in the month of Kartick.

It is conceded by the Commissioner of Income-tax that the hospital and dispensary, when it comes into existence and operation, will be a public charitable trust and the part of the trust income devoted to it will be

exempt from assessment to income-tax. The rules in schedule A provide that during the settlor's lifetime, the hospital and dispensary should be located in a rented house in Deoghar and after her death in Charunibas, the house where she has a right of residence.

The year of assessment is 1939-40 in respect of the accounting year 1938-39. The trustees were assessed upon the whole income of the trust in the sum of Rs. 49,691 for an amount of Rs. 9,061-9-0 tax. The Appellate Assistant Commissioner dismissed an appeal by the assessees against the assessment and, upon reference being made under Section 33 of the Indian Income-tax Act to the Commissioner, he refused to interfere expressing the opinion that the provisions of the trust are inconsistent with a trust of a public character, except with respect to the hospital, and he referred the following question for the opinion of this Court :—

"Whether on a proper construction of the deed of trust, so much of the income of the trust as is not applied for the purpose of constructing and maintaining the female hospital is exempt from tax under the provisions of Section 4 (3) of the Indian Income-tax Act?"

It is not in dispute that "female hospital" in the question includes the dispensary.

The relevant provisions of Section 4 (3) of the Act are :—

"Any income, profits or gains falling within the following classes shall not be included in the total income of the person receiving them :

(i) Any income derived from property held under trust or other legal obligation wholly for religious or charitable purposes, and in the case of property so held in part only for such purposes, the income applied, or finally set apart for application, thereto.

* * * *

In this sub-section 'charitable purpose' includes relief of the poor ....and the advancement of any other object of general public utility but nothing contained in clause (i).........shall operate to exempt from the provisions of this Act that part of the income of a private religious trust which does not enure for the benefit of the public."

The trustees contend that the entire trust is for public religious and charitable purposes and the whole income falls within clause (i) of sub-section (3) of Section 4. The Commissioner's contention is that it is no more than a private religious trust and the income does not enure for the public benefit, save with respect to that part of the income which will be devoted to the hospital and dispensary and to which the latter part of clause (i) applies.

Since the construction of the temple was not completed, the deity and image were not installed and no daily *sheba* and festival had been celebrated, by the conclusion of the accounting year, the question whether the trust is

a public or private one must be ascertained from the provisions of the trust deed.

Since no part of the income of the trust, during the accounting year 1938-39, was devoted to the hospital and dispensary, and since it is conceded that that part of the income which will be devoted to those institutions, when utilised for those purposes, will fall within the exempting clause, the meaning and effect of the trust deed needs to be considered solely with respect to the other trust created by it. The burden is upon the assessees to establish that the income from the trust is exempt from taxation : *vide* the observations of Agarwala, J., at p. 219 in *Commissioner of Income-tax, Bihar and Orissa* v. *Maharaja Visweswar Singh*[1].

Mr. N. C. Chatterjee, for the trustees, contended that the public nature of the entire trust is ascertained from the trust deed, in the following respects:—

1. There is no dedication to a family deity.
2. No portion of the usufruct is reserved to the settlor or to her heirs or members of her family.
3. The family is divested of the *shebaitship*.
4. The majority of the trustees are not members of the settlor's family.
5. The management of the temple is in the hands of a public committee which includes 6 Hindu residents of Deoghar.
6. Daily distribution of food to 95 persons and of periodic refreshment at festivals is to be carried out by the temple committee.
7. No power is reserved in the deed to revoke or vary the objects of the trusts but only the rules in schedule A can be varied.
8. *Pronamis* become part of the trust estate.
9. The public must be informed of the trust property and the accretions thereto.
10. The land upon which the temple is erected has to be consecrated.
11. The public are the beneficiaries of the trust.

It is now convenient to deal with the features of the deed mentioned by Mr. Chatterjee.

1. The settlor's own deity, which she had established in her house, and the image of her own religious preceptor, are to be installed in the temple, which is the purpose of its erection, and the daily *sheba* and festivals to be celebrated by expenditure out of the trust income appertaining to that deity and image. The Nat Mandir, or entrance hall, to the temple is in memory of the settlor's deceased son. Whilst, so far as the settlor is concerned, the perpetuation of the worship of her deity and image and of the memory of her son are pious in the extreme, they are not matters which command public interest. There is no provision in the deed by which

(1) [1935] 3 I.T.R. 216.

members of the public have any right to worship in the temple. See also the observations with regard to (10) *infra.*

2. The deed reserves to the settlor, during her lifetime, the right of residence in Charunibas, which forms part of the trust property, and in which, after her death, the hospital and dispensary will be located. In this respect there is a reservation to the settlor of part of the usufruct. Further, the complete divestment, by the author of a trust, of any interest for himself or herself or for members of his or her family in the property over which a trust is created, does not thereby make the trust a public one.

3. The settlor has reserved to herself the *shebaitship* during her lifetime and thereafter it becomes vested in persons who are strangers in blood. Even so, the object of the trust is clear, namely, to preserve the worship of the settlor's own deity and the image of her religious preceptor.

4, 5, 6, 7. The first trustees are the settlor, the adopted son of her deceased husband and three strangers in blood. Vacancies in the board of trustees are to be filled by the remaining trustees by appointing the senior lineal male descendant of the settlor's deceased husband, if one is available, and other persons from prescribed sects. But, the deed further provides, the settlor reserves to herself the power in her absolute discretion to remove any one or more trustees for misconduct or other reason specified therein, and to fill all vacancies in the board. This, naturally, will apply only during her lifetime. The deed also provides, in the rules contained in schedule A, that the settlor shall be the first managing trustee until her death or retirement. Elsewhere the deed provides that during her lifetime the decision of the settlor at a meeting of the board of trustees shall prevail. The temple committee is comprised of the Jugal Mandir *shebait*, for the time being, (the holder of an office unconnected with the temple) and 6 pious Hindu residents of Deoghar appointed by the trustees, the committee being responsible for the distribution of *prosad* and arrangement and management of periodical worship and ceremonies; but the committee's functions are subject to the supreme control of the trustees. Since the settlor's decision as a trustee prevails at a board meeting and since the administration by the committee is subject to the trustees' supreme control, it follows that, during her lifetime, the settlor will effect entire control over the administration and direction of all matter relating to the temple, including worship, ceremonies and distribution of food, and her wishes and directions will have to be carried out to the same extent as they would have been if there had been no trust created, subject only to such restrictions which the trust imposes, *e.g.*, expenditure and the number of persons to be fed. The feeding of the poor is incidental to the *puja* of a deity and provision in a deed of endowment for this to be carried out does not make a trust anything beyond a private one: vide *Prosad Das Pal* v. *Jagannath Pal* [1] and the

(1) (1932) 37 C.W.N. 181.

observation of Mitter, J., at p. 183, who delivered the judgment of the Court; also vide *Sathappayyar* v. *Periasami*[1] with respect to a *muth*. After the settlor's death the trustees, as a body, will have supreme control and will act by a majority but the discharge of the duties of the committee and the administration of the trust by the trustees will be solely for the purpose of carrying out the wishes and desire of the settlor with respect to the worship and celebration of festivals of her deity and the image of her preceptor. The deed provides that the settlor, during her lifetime, and the trustees, after her death, shall be at liberty at any time to add to, make, vary and repeal all or any of the rules. These rules provide, *inter alia,* for the numbers, qualification, appointment and duties of the members of the temple committee. At any time, its function can be made abortive and have no effect. The incident that a trust is irrecovable does not make it a public one.

8. The deed provides that the *pronamis* and perquisites to be offered to the deities and image shall form part of the trust estate and neither the *shebait* nor anyone else shall have interest or claim in or over the same. This provision does not indicate the creation of a trust in favour of the public but, on the contrary, it denies the right of anyone, which must include any member of the public, having a right to the *pronamis*. In its terms, the deed negatives that benefit is conferred upon the public.

9. The meaning given to the deed of trust by Mr. Chatterjee to support this point rests, as he conceded, on nothing more than the provision for the naming of the trust. This provision does not, in our view, bear the meaning for which he contended. No other term in the deed has been pointed out as containing a requirement, express or implied, that the public must be given information regarding the trust property.

10, 11. The provisions in the deed relating to consecration and their effect do not appear to have been raised before the Income-tax Officer, the Appellate Assistant Commissioner and the Commissioner of Income-tax and no evidence referable to the ceremony of consecration was before them. Nevertheless, considerable importance was sought to be laid upon these matters. The deed requires the trustees "to instal" the deity and the image in the temple "in the manner enjoined by the Hindu *Sastras* and to celebrate within the temple land the founding or the consecration ceremony of the temple and the festival in connection therewith." The deed does not direct consecration of the land which, Mr. Chatterjee contended, is the meaning and effect of the above provision, but consecration of the temple, which ceremony is to be celebrated within the land. He argued that the ceremony to consecrate the land is known as "*prosad utsarga.*" This ceremony and its effect are explained in the Hindu Law of Endowments by the late Pandit Prannath Saraswati; at p. 127 the learned author says:

(1) (1890) I.L.R. 14 Mad. 1.

"The books of ritual contain a direction that before removing the image into the temple, the building itself should be formally given away to the God for whom it is intended. The *sankalpa* or formula of resolve makes the deity himself the recipient of the gift."

Next follows the ritual of celebration and the text continues :—

"It is this ceremony which divests the proprietorship of the temple from the builder and vests it in the image......the *utsarga* is the relinquishment of the donee's right and the gift is completed by the acceptance corporally made by the donee—the image—which is made to take bodily possession of the premises."

The *prosad utsarga* ceremony dedicates a temple to a deity, it does not consecrate the land upon which a temple is erected. It was next contended that, upon the performance of the *prosad utsarga* ceremony, the temple becomes a public one and, consequently, the trust created by the deed is for public charitable purposes. In support of this contention reference was made to a statement at p. 150 in the 2nd Edition of Mr. Ghosh's Law of Endowments which reads as follows :—

"The real criterion of a temple being a public one is the proof of performance of the ceremony known as *prosad utsarga.*"

The authority cited in the text book for this statement is *Gir Har Saroop* v. *Bhagwan Din*[1] in which one of the head-notes to the report contains language identical to that which I have quoted ; reference to page 105 of the judgment in that case shows that this was the evidence given by a witness, which testimony is recited in the judgment and, with respect to it, the judgment continues, it was admitted in that case there was no evidence the ceremony had been performed ; there is no finding or expression of opinion in the judgment as to the correctness of the evidence given by the witness and the head-note is not borne out by the judgment ; there is, therefore, no authority supporting the statement in Mr. Ghosh's text book. Mr. Chatterjee further argued that the provision in the deed for consecration in itself shows the trust is intended to be a public religious trust. Consecration, he argued, is a ceremony restricted to the case of a deity whose worship is to be by the public ; and therefore, he contended, the mere inclusion in the deed of a provision for consecration differentiated the position from that which would exist if a mere private religious trust had been intended. For then, as when a *Thakur* is installed in a private house of a Hindu family, no consecration would, he suggested, be required. As to this, while it may well be the case, that for the installation of a *Thakur* in a private family house no ceremony of consecration is needed, yet neither evidence nor authority has been produced before us to show, that if a private deity is moved to a new temple specially built for his installation, a consecration ceremony of any nature

(1) (1935) A.I.R. 1935 Oudh 96.

cannot appropriately be resorted to. Moreover this aspect of the matter has been referred to in Saraswati's Hindu Law of Endowments (Tagore Law Lectures) at p. 77 in the following passage dealing with consecration :—

"The consecration or *Pratishtha* of the temple, after its construction is completed, forms the subject of separate provisions, although some of them merge on the one hand in the *vastuyaga* and others in the ceremonies attending the consecration of the deity to whom the temple is to be dedicated. For secular purposes, the consecration corresponds to the ceremony of *griha pravesha* or 'house entering.' If the *vastuyaga* has been performed at the beginning of the house (*griharambha*), it is not obligatory to repeat it at the time of the house-entrance (*griha pravesha*) ceremony. *Varaha Mihira* tersely describes the latter thus: 'Amid the shouts of Brahmins the proprietor has to make his entrance into his newly-built house, it being strewed with great many flowers, adorned with archways, and decorated with water-pots filled, the gods being worshipped with incense, perfumes and oblations.'"

Some ceremony of consecration of a type referred to here would seem equally appropriate in respect of a temple for a deity whose worship is to be private as for one whose worship is to be by the public. We have not been informed of any principle of Hindu law incompatible with this view. The English word "consecration" is used in the deed without mention of any particular type of Hindu religious ceremony. There is nothing to suggest that a type of consecration peculiar only to worship by the public is intended in the deed. In view of the other terms of the deed and a consideration of their meaning as a whole we do not consider this provision for consecration carries the matter any further to show an intention to create a public religious trust. Reliance was also placed upon the observation of Sadasiva Aiyar, J., at p. 10, in *Gopala Mooppanar* v. *Subramania*[1] that "temples were intended for the worship of people belonging to all the four castes without exception"; but that observation was made with respect to a temple which undoubtedly was a public one and it does not follow from it that all temples must, of necessity, bear that character. Mr. Chatterjee also referred to *Manohar Ganesh Tambekar* v. *Lakhmiram Govindram*[2] in which the head-note states : "A trust for a Hindu idol and temple is to be regarded in India as one created 'for public charitable purposes' within the meaning of Section 539 of the Code of Civil Procedure (Act X of 1877)." (Section 92 of the Code of 1908). In this report, too, the judgment does not bear out the head-note and a finding, to the effect stated in it, does not appear. Reference to one more decision is now opportune. In *G. Gayaprosad* v. *S. S. Bhargo*[3], Staples, A.J.C., pointed out at p. 50 that, in that case, there was ample evidence to show the temple in question had been all along used for public worship (that would be sufficient to establish it

(1) (1914) 26 I.C. 7. (2) (1887) I.L.R. 12 Bom. 247. (3) (1934) A.I.R. 1934 Nag. 48.

was a public temple); but the learned Additional Judicial Commissioner expressed the opinion, at p. 49, that, whilst a deed by which property was dedicated in favour of a deity did not expressly create a public trust, it certainly did not expressly declare the dedication was meant to be a family or private one, there was nothing in the deed repugnant to the idea that the trust should be to the benefit of the public and in such a case the deed should be interpreted in favour of a public trust; in the light of the evidence given the above opinion is *obiter*; if it were correct then every temple would be a public one if the trust deed did not expressly provide to the contrary even when the public were in no way concerned with it, had never worshipped in it and may have been denied access to it. With respect I am unable to subscribe to the correctness of the opinion of the learned Additional Judicial Commissioner. Assuming however, that it is correct, in the present case there is, in my view, a repugnance in the trust deed to the trust being a public one. The language in the deed makes it clear that the hospital and the dispensary are for the benefit of the public; the dispensary is to be for all persons irrespective of their religion or creed and the hospital for Hindu women (a section of the public). With respect to the other trusts, including the daily feeding, periodical refreshment and free distribution of *bhog*, the deed does not use language by which, expressly or impliedly, those trusts are to be for the benefit of the public or of a section of it. If such was the settlor's intention, she could have used suitable language in the deed but it does not contain words by which such intention can be inferred. Since the public nature of the trust is made clear with respect to the hospital and dispensary but the deed is silent with regard to the temple and the other trust, it can only be inferred that the settlor intended differently with respect to the hospital and dispensary and with respect to the other trusts and there was no intention that those other trusts should benefit the public and be public trusts.

There is no reference, in the deed, to the public or any particular class or sect of it having a right to worship in the temple or even to have access to it. The distribution of the food and refreshment is not directed to be made to the public. The hospital and dispensary are to be located in a separate building from the temple, which, incidentally, is an additional indication that the public nature of the trust is to be confined to the purposes of those institutions. The main characteristic of a public temple is that it is intended for the use of the public at large or a specified class, who are entitled to the right of worshipping in it. No such intention or right is found in the trust deed. In *Nabi Shirazi* v. *Province of Bengal* [1], in respect of a public temple, Mitter, J., observed at p. 228 that "the beneficial interest must be vested in an uncertain and fluctuating body of persons—either the public at large or some considerable portion of it answering a

(1) I.L.R. [1942] 1 Cal. 211.

particular description." The trust deed does not vest any beneficial interest either in the public at large or in a particular section of it.

The deed reflects that the settlor intended to provide, upon a generous scale, for the observance of the daily worship and celebration of festivals of her private deity, which she had established, and of the image of her religious preceptor. She also perpetuated the memory of her deceased son by erecting to him the Nat Mandir adjacent to the temple. The public has no interest in those objects. There is no grant in favour of the public to receive the food and other refreshment which is to be distributed or to have a right to worship in the temple or even to have access to it. The trust, which the settlor created with respect to the temple, its erection and all matters and things appertaining to it, is a private trust and is not one for public charitable purposes.

At the commencement of his opening on behalf of the trustees Mr. Chatterjee stated this reference originally came before the Chief Justice and Panckridge, J., and after it had been argued for some time, the learned Chief Justice suggested that the matters arising out of it should be discussed between the assessees and the Income-tax authorities; and an adjournment was granted for that purpose. Mr. Chatterjee produced a deed which, he said, had now been executed by the settlor placing the question beyond doubt and making it clear the whole trust is for public charitable purposes. Dr. Gupta, for the Commissioner, objected to this deed being placed before us, contending that the reference must be decided upon the deed and the position which existed during the accounting year; the assessment for the year 1939-40 is the only matter arising for decision; any subsequent alteration by means of a later deed cannot affect that position; and the deed can only be operative from the date it was made. Agreeing with his submission, that the deed cannot have retrospective effect, we refused to allow it to be placed before us.

The burden is upon the assessees to show that the income of which they are in receipt and in respect of which they are charged to tax under Section 3 of the Act, is exempted from taxation. They have failed to discharge this burden and in my opinion the question in this reference should be answered in the negative.

There will be no order as to costs.

ORMOND, J.—Having had the opportunity of seeing in writing before its delivery the judgment which has been delivered by my learned brother I need say no more than that I entirely agree and have nothing to add.

Reference answered in the negative.

[IN THE CALCUTTA HIGH COURT.]

COSSIMBAZAR RAJ WARDS ESTATE

v.

COMMISSIONER OF INCOME-TAX, BENGAL.

GENTLE and ORMOND, JJ. February 14, 1946.

INDIAN INCOME-TAX ACT (XI OF 1922), SECS. 4 (3) (vii), 12—INCOME AND CAPITAL—ROYALTY—MINING LEASE—PAYMENT MADE TO LESSOR ON SURRENDERING COAL MINES—WHETHER CONSIDERATION FOR TERMINATING LEASE OR ROYALTY ON ABANDONED COAL—WHETHER LIABLE TO INCOME-TAX.

The Cossimbazar Raj Estate had granted to a company in 1916 a mining lease of some colliery lands in the estate. The lease was for a period of twenty years, but the lessees were at liberty to abandon the lands at any time before the period of the lease expired provided they paid up in full the rents and royalty of every description due to the lessor at the time of abandonment. In 1919 the lessees assigned the lease to another company with the consent of the lessor. In 1933, during the currency of the lease of 1916, the assignees entered into an agreement with the lessor by which they undertook to continue to hold the lease and the areas demised, and to be bound by the terms and conditions of the lease of 1916 so long as coal remained workable. The agreement further provided that if any coal remained unworked for any reason whatsoever royalty should be payable in the same manner as if the coal had been worked, as soon as the coal should have been abandoned. In 1939 when there still remained unworked coal in the mines the lessees surrendered to the lessor the coal mines and rights granted by the lease of 1916 and the agreement of 1933 and paid to them a sum of Rs. 1 lakh in full satisfaction of all their claims against the lessees. In assessing the estate to income-tax the Income-tax authorities included the sum of Rs. 1 lakh, under Section 12 of the Income-tax Act, as royalty on unworked coal. It was contended on behalf of the estate that the payment was made for the purchase price of the right to relinquish the lease and the agreement and as such it was either a capital receipt or was a casual receipt within the meaning of Section 4 (3) (vii) of the Act:

Held, *that on a consideration of the substance of the transaction, it was clear that the estate did not receive the payment of Rs. 1 lakh as consideration for terminating the lease and the agreement, but as royalty on abandoned coal pursuant to a term in the agreement and as such it was assessable to income-tax.*

Malleti v. *The Staveley Coal and Iron Company Ltd.* [*1928*] (*13 Tax Cas. 772*) and *Van den Berghs Ltd.* v. *Clark* [*1934*] (*19 Tax Cas. 390*) distinguished.

Cases referred to :—

Anglo-Persian Oil Co., Ltd. *v.* Dale [1931] (16 Tax Cas. 253 ; [1932] 1 K.B. 124 ; 100 L.J.K.B. 504 ; 145 L.T. 529 ; 47 T.L.R. 487).

British Insulated and Helsby Cables Ltd. *v.* Atherton ([1926] A.C. 205 ; 95 L.J.K.B. 336 ; 134 L.T. 289 ; 42 T.L.R. 187 ; 10 Tax Cas. 155).

Commissioner of Income-tax, Madras *v.* Messrs. Harveys Ltd. [1940] (8 I.T.R. 307).

Commissioners of Inland Revenue *v.* Newcastle Breweries Ltd. [1927] (96 L.J.K.B. 735 ; 43 T.L.R. 476 ; 137 L.T. 126 ; 12 Tax Cas. 927).

Commissioners of Inland Revenue *v.* North Fleet Coal and Ballast Co., Ltd. [1927] (12 Tax Cas. 1102).

Glenboig Union Fireclay Co. *v.* Commissioners of Inland Revenue ([1922] Sess. Cas. (H.L.) 112 ; 59 Sc. L.R. 162 ; 12 Tax Cas. 427).

Gliksten and Son Ltd. *v.* Green ([1929] A.C. 381 ; 98 L.J.K.B. 363 ; 140 L.T. 625 ; 45 T.L.R. 274 ; 14 Tax Cas. 364).

John Smith and Son *v.* Moore ([1921] 2 A.C. 13 ; 58 Sc. L.R. 313 ; 90 L.J.P.C. 149 ; 125 L.T. 481 ; 37 T.L.R. 613 ; 12 Tax Cas. 266).

Mallett *v.* Staveley Coal and Iron Company Ltd. ([1928] 2 K.B. 405 ; 97 L.J.K.B. 475 ; 139 L.T. 241 ; 13 Tax Cas. 772).

Sunderland Shipbuilding Co., Ltd. *v.* Commissioners of Inland Revenue [1926] (12 Tax Cas. 955 ; 136 L.T. 689).

Van den Berghs Ltd. *v.* Clark [1934] (19 Tax Cas. 390 ; 153 L.T. 171 ; 51 T.L.R. 393 ; 104 L.J.K.B. 345 ; [1935] A.C. 431 ; 3 I.T.R. Eng. Cas. 17).

Reference under Section 66 (1) of the Indian Income-tax Act (XI of 1922) by the Income-tax Appellate Tribunal : Income-tax Reference No. 2 of 1945.

STATEMENT OF CASE.

"This is an application under Section 66 (1) of the Income-tax Act made by Maharaja Sris Chandra Nandy of Cossimbazar asking us to refer to the High Court of Judicature at Fort William in Bengal certain questions of law, said to arise out of the order under Section 33 made by the Calcutta Bench of the Tribunal, dated the 29th February 1944, relating to the applicant's assessment to income-tax for the year 1940-41.

2. The facts of the case may be briefly stated. On the 1st Sraban, 1315 B. S. the Bengal Nagpur Coal Co., Ltd., obtained from the late Maharaja Sir Manindra Chandra Nandy of Cossimbazar a fifteen years' lease in respect of coal areas in moujas Gangutia and Chhotadhamua. In 1304 B. S. Dr. Shircore obtained a lease in respect of some other coal areas in mouja Chhotadhamua. After the death of Dr. Shircore and the expiry of his lease his executors obtained permission in Baisakh 1317 to cut the coal pillars in the upper seam of the area comprising 180 bighas. Other seams in the same area were in the khas possession of the Cossimbazar Estate. The Bengal Nagpur Coal Co., Ltd., obtained a twenty years' lease on the 9th Aswin 1323 B. S., corresponding to the 25th September 1916, in respect of other seams in the 180 bighas area which were in the khas possession of the Cossimbazar Estate. This lease of the 25th September 1916 was a consolidated pattah in respect of moujas Gangutia and Chhotadhamua covering the first lease of Sraban 1315 and the fresh lease in respect

of the additional area in Chhotadhamua. The Company thus got the right to work all seams of the areas concerned with the exception of the upper seam in the 180 bighas area of Chhotadhamua.

3. On the 12th February 1919, the Bengal Nagpur Coal Co., Ltd., transferred their interest under the lease of the 25th September 1916, with the consent of the Maharaja, to the Bengal Coal Co., Ltd. On the 24th April 1933, an agreement was made between the Manager, Cossimbazar Wards Estate and the Bengal Coal Co., Ltd., providing that during the lifetime of Maharaja Sir Manindra Chandra Nandy the Bengal Coal Co., Ltd., became the lessee in place of the Bengal Nagpur Coal Co., Ltd. The Bengal Coal Co., Ltd., was deemed to continue to hold the lease between the Estate and the Bengal Nagpur Coal Co., Ltd., and to be bound by the terms and conditions of that lease which would be deemed to be renewed as long as any coal (excepting some coal specified) remained workable.

4. The lease dated the 25th September 1916 provided *inter alia* that the Company shall be at liberty to abandon the lease at any time before the period expired provided the Company paid up in full the rents and royalty of every description due to the estate up to the time of abandonment and no objection would be made to that effect. There were also conditions in the lease restricting the manner of working the collieries, and providing for pillars of specific girth at distances to keep the upper seam free from any danger of collapse. The agreement of the 24th April 1933, altered the original condition that the Company could give up the lease at any time provided rents and royalty of every description were paid up to the date of abandonment, and it was agreed that if any coal remained unworked for any reason royalty would be payable to the lessor in the same manner as if the coal had been worked, as soon as the said coal should have been abandoned or rendered inaccessible in the remaining course of working. (We may mention here that the Appellate Assistant Commissioner seemed to think that the option to surrender the lease at any time before its expiry according to the 1916 deed was conditional on the payment of rent and royalty for the entire period of the lease. This does not appear to be correct as stated above).

5. The area worked by the Company contained 3 seams known as Dishergarh, Hathnol and the Sanctoria, being the top, middle and lower seams respectively. The top seam was extensively mined and there was practically no coal left. The middle seam, where the coal was of an inferior quality, was not at all worked. The lowest seam contained good coal and the company was interested in working this seam only. Hathnol and Sanctoria (the middle and the lower) seams being within a short distance of each other, depillaring operations in the lower seam might have brought about a collapse of the Hathnol seam just above it, unless sufficient

care was taken. The 1916 deed gave the Company right of pillar-cutting provided it paid *salami* of Rs. 75 per bigha. *Salami* was paid and pillar-cutting operations were taken in hand without waiting for the formal sanction.

6. It appears that the estate was not satisfied about the operations which were proceeded with by the Company. The Court of Wards in charge of the Cossimbazar Estate intimated to the Company that it had not been granted any sanction, inasmuch as no joint measurement had been made as was provided for in the deed of agreement of the 24th April, 1933, that the Company's method of extracting and splitting of pillar in the Sanctoria seam damaged the Hathnol seam which was just above it, besides causing considerable loss in the Sanctoria seam itself, and that the estate did not, therefore, approve of the operations which were being carried out by the Company. The Court of Wards further informed the Company that its depillaring operations were wholly unauthorised and were immensely detrimental to the interests of the estate and that the estate would have to take necessary steps for stopping further pillar-cutting if the matter was not settled forthwith. The Court of Wards also warned the Company that it would be held responsible for all losses of coal that had already been caused or would be caused by unauthorised pillar extraction carried on in a manner not approved of by the estate. The matter of pillar-cutting was subsequently referred to Mr. M. M. Mukherjee, General Manager and Agent of Messrs. Martin & Co.'s Collieries. Through Mr. Mukerjee's intervention the pillar extraction work was suspended and a settlement appears to have been negotiated. Ultimately a conference of the representatives of both sides including the expert, Mr. Mukerjee, was held on the 18th July 1939, as a result of which an instrument of surrender was drawn up on the 21st September 1939. It was agreed that the Company should be at liberty to relinquish and to determine the said pattah of the 25th day of September 1916, and the agreement of the 24th day of April 1933, and the coal mines, seams and premises therein comprised together with all surface rights granted thereunder or held and enjoyed therewith with effect from the 18th day of July 1939 in consideration of the following conditions to be observed and performed by the Company :—

"(1) that the Company should pay a sum of Rs. 1 lakh to the Court of Wards and the Court of Wards should accept the same in full satisfaction of all their claims against the Company and should not make or have any further claim of any sort or description in respect of the mines, seams, lands and premises described in the said schedule hereto and/or under the pattah and the agreement hereinbefore recited or any of them."

7. This sum of Rs. 1 lakh was brought under assessment by the Income-tax Officer. The Appellate Assistant Commissioner, Calcutta,

Range A, found "no reason for excluding it from the assessment." The Appellate Assistant Commissioner said that "Nothing has been pointed out to me to show that the Company offered any amount for any loss actually caused while on the other hand, the manager's letter shows that the offer was for the estate's right to receive royalties on the coal of Sanctoria seam and surrender of Hathnol." He further proceeded that "the expert made a report but found no damage done except a small encroachment which also was considered doubtful. The term of one lakh was considered reasonable in view of what coal was estimated to be available in the various seams ...." The Appellate Assistant Commissioner further observed :—

"This amicable settlement can have only one meaning which is that there was no loss and if there was any threat of a loss, the threat was removed; and if there are mutual complaints of losses, they are balanced; and the entire payment was estimated royalty payable under agreement."

8. The matter was then brought up in second appeal before the Appellate Tribunal. The Bench that heard this appeal observed as follows :—

"The appellant contends that this receipt cannot be assessed as it has been received on the breach of contract by the Company and for waiving the right of forfeiture of the lease and as consequential damages. It is further contended that the compensation was paid by the Company for loss caused to the estate by depillaring operation of the Company and this payment was for loss caused to the property of the appellant and the payment therefore is not any income assessable. It is also contended that this is a casual receipt and does not arise out of any business, profession or vocation and is exempt under provisions of Section 4 (3) (vii) of the Income-tax Act and therefore exempt from taxation."

The Bench held that—

"This sum of Rupees one lakh has been assessed as royalty received in the accounting year in terms of the agreement. Apparently by the surrender of the lease the Company had given up the working of the mines any further and as this giving up of the working of any further coal has not arisen out of any geological disturbance or any necessary provision for protection, the royalty thereon of such unworked coal was immediately payable as soon as the working of coal was abandoned under clause 7 of the deed dated the 24th April 1933. The fact that it was stated to be royalty and that it was the royalty on the remaining coal in the seam abandoned makes it very clear that the amount was received by the assessee as royalty on coal which the company had to pay in terms of the agreement........... The source of this receipt is the agreement dated the 24th April 1933 and the covenant that in case of any abandonment the royalty on the amount of abandoned coal should be payable and that forthwith. It is only in

pursuance of this agreement that the quantity of coal available was estimated and the settlement was reached in regard to the amount that was so due."

"As regards the contention that it is compensation for loss caused to the assessee we find there is absolutely no material..........."

"........The receipt arises out of the terms of the covenant. It is a receipt that had been provided for and, therefore, cannot be held to be a casual receipt."

For these and other detailed reasons mentioned in the order under Section 33 of the Bench of the Tribunal that heard this appeal, it came to the conclusion that it was "unable to accept the appellant's contention that the receipt is not assessable."

9. On these facts the following questions of law were formulated for reference to the Honourable High Court:—

"(a) Whether the sum of Rs. 1,00,000 received by the Cossimbazar Raj Wards Estate from the Bengal Coal Co., Ltd., was assessable to income-tax under the Indian Income-tax Act?

(b) Whether the said sum was at all royalty and, as such, income within the meaning of the Indian Income-tax Act?

(c) Whether for the decision of the question whether the said sum was compensation for loss caused to the appellant's estate, the basis of the claim as made by the appellant and met by the Bengal Coal Co., Ltd., or actual damage caused to the estate is the relevant consideration?

(d) Whether the said receipt was provided for by the terms of the deed of agreement dated the 24th April 1933, and if so, whether an anticipatory provision would be a bar to the said receipt being considered a receipt of a casual and non-recurring nature within the meaning of Section 4 (3) (vii) of the Indian Income-tax Act?

(e) Whether the inclusion of the private income of the Maharaja in the income of the Wards Estate for the purpose of assessment of the said Wards Estate was justified in law?"

10. The respondent (Commissioner of Income-tax, Bengal) sent in a written reply to the application for reference in accordance with rule 54 of the Appellate Tribunal Rules. The learned Commissioner stated that the questions formulated arose out of the Tribunal's order and that they were questions of law. It, however, appeared to him that as only two points were really involved, *viz.*, (1) whether the sum of Rs. 1,00,000 was assessable income and (2) whether the inclusion in the assessment of the Maharaja's private income was correct in law, only two questions might be referred to the High Court. He framed the following two questions:—

"(1) Whether in the facts and circumstances of the case the sum of Rs. 1 lakh received by the Cossimbazar Raj Wards Estate from the Bengal Coal Co., Ltd., was, in law, assessable to income-tax,

(2) Whether the inclusion of the private income of the Maharaja in the income of the Wards Estate for the purpose of assessment of the said Wards Estate was justified in law."

11. Before us, however, question marked (e) above among the applicant's questions, namely, "Whether the inclusion of the private income of the Maharaja in the income of the Wards Estate for the purpose of assessment of the said Wards Estate was justified in law," was not pressed, and was withdrawn in writing, evidently because although it might be a question of law, it would be simply answered against the appellant. In any case, we need not now discuss this matter further.

12. The learned representatives of the applicant agreed that the one question formulated by the learned Commissioner, in place of questions (a), (b), (c) and (d) of the applicant, might do. We agree that this is the proper course to follow in this case. In the circumstances, we refer for the decision of their Lordships of the High Court of Judicature at Fort William in Bengal the following question of law :—

"Whether in the facts and circumstances of the case the sum of Rs. 1 lakh received by the Cossimbazar Raj Wards Estate from the Bengal Coal Co., Ltd., was, in law, assessable to income-tax ?"

R. B. Pal and *B. L. Pal*, for the assessee.

S. K. Gupta and *J. C. Pal*, for the Commissioner.

JUDGMENT.

GENTLE, J.—This is a case stated by the Income-tax Appellate Tribunal under Section 66 of the Indian Income-tax Act at the instance of the assessee, who is the manager of the Cossimbazar Raj Estate appointed by the Court of Wards. The question which this Court is required to consider is :—

"Whether in the facts and circumstances of the case the sum of Rs. 1 lakh received by the Cossimbazar Raj Wards Estate from the Bengal Coal Co., Ltd., was, in law, assessable to income-tax ?"

The estate of the Maharaja of Cossimbazar has been in the management of the Court of Wards since about the year 1920 or 1921. A portion of the estate comprises some colliery lands in Moujas Gangutia and Chhotadhamua. On the 25th September, 1916, prior to the Court of Wards taking charge, the Maharaja granted, by a Bengali *pattah*, a mining lease of that property to the Bengal Nagpur Coal Co., Ltd., upon, *inter alia*, these terms :—

(1) The lease to be for a period of 20 years from date;

(2) The lessees would have the right of raising coal from the lands for which they should pay the royalty specified in the lease;

(3) The lessees should be at liberty to abandon the lands at any time before the period of the lease expired, provided they paid up in full the rents

and royalty of every description due to the lessor at the time of abandonment;

(4) The lessees to keep coal pillars of specified dimensions and at stated intervals in the mines; and

(5) The lessees had an option to renew the lease at its expiration on the same terms, if coal still was unfinished.

On the 12th February, 1919, the lessees assigned the lease to the Bengal Coal Co., Ltd., with the sanction and approval of the lessor. Thereafter, that Company raised coal from the lands and paid the stipulated royalty to the lessor and, later, to the manager of the Court of Wards when the estate came under its jurisdiction.

During the currency of the lease of 1916, an agreement, dated the 24th April, 1933, was made between the estate manager appointed by the Court of Wards and the Bengal Coal Co., Ltd., by which it was, *inter alia*, agreed that :—

Clause (3). The Company would apply for and would be granted pillar-cutting rights in such areas as required upon payment of specified *salami*;

Clause (6). The Company undertook, notwithstanding anything to the contrary contained in the lease of 1916, to continue to hold the lease and the areas thereby demised and to be bound by the terms and conditions of the lease which should be deemed, if and as necessary, to have been renewed so long as any coal remained workable;

Clause (7). In the event of any coal remaining unworked for any reason whatsoever (otherwise than as provided in clause 6 and to which reference is not material), royalty thereof should be payable to the lessor in the same manner as if the coal had been worked, as soon as the said coal should have been abandoned;

Clause (8). Save and except clauses (4), (30) and (31) of the lease of 1916 (to which reference is unnecessary) all other terms and conditions laid down therein should remain in force as if no agreement (of the 24th April, 1933) had been executed.

The colliery comprised three seams: Dishergarh the upper seam; Hathnol the middle seam; and Sanctoria the lower seam. Dishergarh had been worked out by 1933, when the agreement in that year was made, Hathnol contained inferior coal and no working took place in that seam after the 1933 agreement. Thereafter working was confined to Sanctoria, which is below Hathnol. About 1939 the coal in the Sanctoria was running out and, substantially, there remained only the coal pillars which had been left pursuant to the terms of the 1916 lease. In that year the Company applied for pillar-cutting rights of those pillars and paid the required *salami* which was accepted by the manager. No formal permission to cut was given. The Company thereupon commenced raising the remaining

coal in Sanctoria, which was confined to the pillars which had been erected, and with respect to which they had applied for pillar-cutting rights.

On the 16th June, 1939, Mr. J. N. Sirkar, the estate manager appointed by the Court of Wards, wrote to his superior, the Commissioner of the Presidency Division, Calcutta. The letter states as follows:—

"The Company had applied for pillar-cutting rights; they had paid the required *salami*; formal permission had not been given but the Company contended that permission should be considered as having been granted immediately the *salami* was paid and they had commenced pillar-cutting; this was being done in a manner which had not been approved by Mr. Carver, (apparently the Court of Wards' Consulting Engineer) as the method was unsound and dangerous as it would render Hathnol unworkable; the Company was depillaring the area in spite of protests and the only way to stop this being done was by means of costly litigation; after consulting the Maharaja, Mr. M. M. Mukherjee had been appointed to take up the matter for a settlement, favourable to the estate, out of Court. Elsewhere in the letter the manager wrote that the Company undertook to continue to hold the leases and the areas demised and to be bound by the terms and conditions of the original *pattah* so long as coal remained workable and the agreement provided that in the event of relinquishment whilst coal still remained unworked for any reason whatsoever, royalty would be payable to the estate for the coal left unworked. The letter adds that, with a view to escaping liability to pay for the loss caused to the estate, the Company proposed to pay one lakh of rupees for the estate's right to receive royalty on the coal of Sanctoria and Hathnol seams; the proposal had been examined; Mr. Carver had reported that, in respect of the remaining coal in Sanctoria and Hathnol seams, royalties on these two seams approximated to Rs. 2,28,000 and the Company had been asked to pay Rs. 1,50,000 but they had refused to do so.

On the 7th July, 1939, Mr. M. M. Mukherjee wrote to the Court of Wards Manager regarding a visit he had paid to the collieries where he had interviewed Mr. Barraclough, who represented the Company. He had expressed objection to that gentleman to the pillar-cutting and had told Mr. Barraclough the legal steps which they contemplated taking in order to stop the work; Mr. Barraclough said that he was confident of the Company's right to continue. The letter adds:—

"I also felt that his contention was probably right irrespective of the consequence."

Ultimately the matter was settled by an instrument of surrender and relinquishment, dated the 21st September, 1939, made between the Company and the manager by which the Company paid to the Court of Wards a sum

of one lakh of rupees and the instrument witnessed that the Company thereby surrendered and relinquished to the Court of Wards all the coal mines, seams, lands and rights granted by the lease of 1916 and the agreement of 1933 and the Court of Wards released, discharged and absolved them from all obligations, claims, demands and liabilities arising thereunder. The Company vacated the coal mines, and, at the time they did so, there still remained, in Sanctoria and Hathnol seams, coal which was unworked and which the Company had abandoned.

In the assessment to tax upon the income of the estate, for the year 1940-41, the above sum of one lakh of rupees was included, under Section 12, as the amount of royalty on unworked coal. The assessee, the manager of the estate, appealed to the Appellate Assistant Commissioner and from him to the Income-tax Appellate Tribunal both appeals being dismissed. On application by the assessee the case was stated by the Tribunal which is now the subject of consideration.

On behalf of the assessee Dr. Pal conceded that, if the payment of one lakh of rupees was for royalty in respect of the abandoned coal in the collieries at the time the company ceased to work there, that sum is properly assessable to income-tax under Section 12. He contended, however, that the payment was not made for royalty but was for the purchase of the right to relinquish the lease and agreement and this is the price for the relinquishment. As such, he argued, it is either a capital receipt or is a casual receipt within the contemplation of Section 4 (3) (vii) of the Income-tax Act and, in either event, it is not liable to be assessed to tax.

The question whether receipts and payments are attributable to capital or to yearly trading or income has been the subject of several decisions many of which were mentioned and to some I propose to refer. In the case of *Van den Berghs Ltd.* v. *Clark* (*H. M. Inspector of Taxes*)[1] there was an agreement between two rival manufacturers of margarine for friendly alliance between them and for sharing their respective profits; the House of Lords held that such agreement was not an ordinary commercial contract usually made to carry on their trade and a receipt by one party from the other in consideration of the termination of the agreement was a capital receipt. In *British Insulated and Helsby Cables, Ltd.* v. *Atherton*[2] the House of Lords held that the sum provided as a nucleus of a pension fund for employees was a capital receipt; a similar decision regarding the payment by a coal merchant for the acquisition of a right to a number of current contracts to supply coal is found in *John Smith & Son* v. *Moore*[3]. Similarly, a sum received by a fireclay company as compensation for leaving unworked fireclay under a railway was held to be a capital receipt: *Glenboig Union*

(1) (1934) 19 Tax Cas. 390 ; 3 I.T.R. Eng. Cas. 17.
(2) [1921] A.C. 205 ; 10 Tax Cas. 155.
(3) [1921] 2 A.C. 13 ; 12 Tax Cas. 266.

Fireclay Co. v. *Commissioners of Inland Revenue*[1]. On the other hand, in *Commissioners of Inland Revenue* v. *Newcastle Breweries, Ltd.*[2], compensation paid to a brewery company for requisitioned stock was held to be a trade or income receipt. Similarly, the sum paid to a ship-builder for cancellation of a contract to build a ship was held to have been received in the ordinary course of the company's trade: *Sunderland Ship-building Co., Ltd.* v. *Commissioners of Inland Revenue*[3]; likewise, a lump sum received by a quarry company, in lieu of four annual payments, as consideration for relieving a customer of his contract for ten years: *Commissioners of Inland Revenue* v. *North Fleet Coal and Ballast Co., Ltd.*[4] A sum recovered from an insurance company in respect of the destruction of a timber company's stock was held to be an income receipt: *J. Gliksten and Son, Ltd.* v. *Green*[5].

Dr. Pal particularly relied upon *Mallett* v. *Staveley Coal and Iron Co., Ltd.*[6] In that case a company held two mining leases; the earlier one of 1882 empowered the company to surrender the whole, but not a part, of the demised property; the lease of 1919 conferred no power whatever of surrender; in 1922 the company agreed with the lessor for a surrender of a part of the lands demised in the 1882 lease and the whole of the lands demised by the 1919 lease and it was held that such payment was a capital expenditure and not a payment out of income.

From the authorities, to which reference has been made, the nature of the payment is dependent upon the particular facts of each case and I now turn to the facts of the present case. Under the lease of 1916 the lessees were entitled to abandon the colliery lands at any time during its currency provided they paid all royalties and rents due at the time of relinquishment or abandonment; the lessor could not require any payment beyond the amount due under the lease, as consideration for its termination. Before the expiration of the 1916 lease and, it would follow, before the lessees had exercised the option to continue, which was contained in that lease, the agreement of 1933 was made which as I see it, in effect was a fresh demise upon the terms contained in the earlier lease subject to certain modifications expressed in the later agreement. The period of the later grant was not expressed in terms of years but was for a period during which coal remained in the lands which could be worked. One of the terms, in clause 6 of the agreement, is that the Company, who are the lessees, undertook, notwithstanding anything to the contrary contained in the lease of 1916, to continue to hold the lease and areas thereby demised so long as any coal remained workable. Dr. Pal argued that this term cancels or expressly negatives the

(1) [1922] Sess. Cas. (H. L.) 112; 12 Tax Cas. 427.
(2) (1927) 12 Tax Cas. 927.
(3) (1927) 12 Tax Cas. 955.
(4) (1927) 12 Tax Cas. 1102.
(5) [1929] A.C. 381; 14 Tax Cas. 364.
(6) (1928) 13 Tax Cas. 772.

term in the lease entitling the lessees to terminate the contractual relationship at any time. He contended that the lessees were bound to continue the agreement until all coal had been, in fact, raised or worked out and, until that event occurred, they had no right under the agreement to terminate the contractual relationship. Consequently, he further argued, the lessor was in a position to demand a payment in consideration for permitting the lessees to terminate, relinquish or abandon and, without that permission, the lessees had no right to cease working the colliery; one lakh of rupees was a payment for this permission and was received as consideration for the termination of the agreement; it was not a payment of royalty in respect of the coal abandoned in the colliery but was a capital receipt.

Clause 6 of the agreement expressly provides that the lessees were to be bound by the terms and conditions of the lease. Clause 8 incorporates, by reference, all the terms and conditions contained in the lease (except three terms which are immaterial for the present consideration), and the clause does not exclude the term entitling the lessees to abandon the lands at any time. Clause 7 provides that if any coal remained unworked for any reason whatsoever royalty should be payable in the same manner as if the coal had been worked, as soon as the coal should have been abandoned. When, by reference to it, the terms of one contract are incorporated into another contract, those terms are the terms of the other contract subject to any term contained in the latter. Clauses 6 and 8, more particularly clause 8, embody the abandonment term of the lease as a term of the agreement. Then clause 7 must be examined. That clause required payment of royalty in respect of coal abandoned for any reason whatsoever. That is an express term, to which the embodied abandonment term from the 1916 lease is subject. When these two are read together it is clear that the lessees were entitled to terminate the agreement at any time but they were required, upon abandonment or termination, to pay royalties upon all coal which remained unworked, in addition, as under the lease, to paying any royalty or other amounts due to the lessor at that date. The agreement did not, in my view, cancel or withdraw the right which the lessees had under the lease of termination at any time but expressly, by incorporation of the terms of the lease, continued that right which was one enuring to them under the agreement but there was an additional liability, in the event of it being exercised, namely, payment of royalty in respect of the coal still remaining in the mines.

In my opinion, the agreement, instead of specifying its term by a period of years, was for such time during which coal remained to be worked. The word "undertakes," in clause 6, did not prevent the lessees from availing themselves of the term of the lease embodied in the agreement, to terminate at any time. But if they did so they were required

under the agreement to pay for abandoned coal as well as to pay the dues in respect of royalties which were recoverable at that time. In those circumstances the lessor was not in a position to require a payment in consideration of, or for permission for, earlier termination of the agreement. The lessees had that right, provided they fulfilled the terms in the lease, to leave at any time and having that right there was no need for them to purchase that right. The circumstances in the present case are clearly distinguishable from those in *Mallett's case*[1]. There, there was no right under the lease to determine during the currency of one lease and, in regard to the other lease, to determine or surrender a portion of the whole. Consequently, when the lessees required and wished to surrender, the lessor was then in a position to demand a sum of money as consideration for permitting a surrender. Here, the lessees always had the right to determine at any time.

The Tribunal has found, as a fact, that the sum of one lakh of rupees was paid to the assessee as royalty on abandoned coal. The facts appear in the two inter-departmental letters, previously mentioned. From those letters it emerges that the estate's officers were not satisfied that the lessees were doing anything which infringed the terms of the agreement by raising coal by means of pillar-cutting, which was the sole matter of complaint and of a potential claim. The lessees offered one lakh of rupees for the estate's right to receive royalties in future which, in my view, was an offer of payment of royalty in respect of abandoned coal upon ceasing to work the mines. Thereupon the estate's officers ascertained approximately the amount of that royalty was Rs. 2,28,000 and an offer to accept Rs. 1,50,000 was made. A reduction can well be understood, inasmuch as the unworked coal would remain in the seams and be available for future work. I appreciate fully that it does not always follow that when an amount of a payment is calculated upon the basis of what would be due under an agreement, the sum so ascertained is necessarily a payment pursuant to the agreement but, in this case, I am satisfied that the payment of one lakh of rupees was one which came within the terms of the agreement. The findings of fact, expressed by the Appellate Tribunal, are binding upon us provided there was evidence to justify the findings. Here, the facts are to be ascertained from the construction and interpretation of the two inter-departmental letters.

In my view the Tribunal has correctly construed and interpreted those letters. The substance of the transaction must be considered and, when that is done in this case, it is clear that the assessee did not receive the payment of one lakh of rupees as consideration for terminating the lease and the agreement but as royalty on abandoned coal pursuant to a term in the agreement. It was appreciated, as appears from Mr. M. M. Mukherji's

(1) (1928) 13 Tax Cas. 772.

letter, that a claim in respect of wrongful working of the mines was unlikely to be established and the payment which could be demanded from the lessees would have reference only to royalty upon abandoned coal—a payment which falls within clause 7 of the agreement. In my view, the present case is covered by the latter part of the observations of Lord Macmillan in *Van den Berghs, Ltd.* v. *Clark* [1], where, in the course of his speech he said, as reported at page 431 :—

"Now what were the appellants giving up? They gave up their whole rights under the agreements for 13 years ahead. These agreements are called in the stated case 'pooling agreements', but that is a very inadequate description of them, for they did much more than merely embody a system of pooling and sharing profits. If the appellants were merely receiving in one sum down the aggregate of profits which they would otherwise have received over a series of years, the lump sum might be regarded as of the same nature as the ingredients of which it was composed."

That passage has been cited with approval in *Commissioner of Income-tax, Madras* v. *Messrs. Harveys, Ltd.*[2] In my view, the latter part of that observation has direct reference to the present case. In the *North Fleet Coal and Ballast Co.'s case* [3], to which I have previously referred, there was a contract, subsisting for ten years, for the sale of chalk and also for the building of a wharf. It was agreed between the quarry company and the purchaser that in consideration of the payment of £ 900 yearly for the remaining four years of the term the purchaser should be relieved of his liability ; subsequently the company accepted a lump sum payment of £ 3,000 in lieu of the annual payments; it was held that the payment of £ 3,000 was chargeable to excess profits duty as a trading profit as it represented profits in a new form and it was tantamount to income. In the present case, if the lessees had continued to work the seams and raise coal, the assessees would have obtained the royalty in respect of that coal. Instead of that, a sum has been paid with respect to that royalty pursuant to a term in the agreement which required it to be paid at once in the event which has happened. In my view, that can be only a receipt by way of income or profit. This payment was contemplated and provided for by clause 7 of the agreement and it was anticipated, it cannot, in the circumstances, be a casual receipt.

There is one matter which remains for which a few observations are required. The instrument of surrender dated the 21st September, 1939, recites the lease and the agreement and other matters and then there is a recital of an agreement, made shortly prior to the date of the instrument, by which it was agreed that the company should be at liberty to relinquish and determine the lease and the agreement with effect as from the 18th

(1) (1934) 19 Tax Cas. 390 ; 3 I.T.R. Eng. Cas. 17.
(2) [1940] 8 I.T.R. 307.
(3) (1927) 12 Tax Cas. 1102.

July, 1939, and that the company should pay a sum of one lakh of rupees to the Court of Wards which the Court of Wards should accept in full satisfaction of all their claims against the company. Later the deed witnessed, as previously I have set out.

Dr. Pal argued that the nature of the payment should be ascertained from the contents of the surrender deed and from which he contended, it is clear that one lakh of rupees was received in consideration for the termination of the agreement of lease. That is not as I read the instrument. The payment is expressed to be made in satisfaction of the claims by the Court of Wards. Nowhere is the payment expressed to be with respect to the termination of the lease and agreement. The claim made was with respect to the royalty upon coal which was abandoned and that claim is included in the word "claims" in that part of the recital to which reference has been made. As I have said previously the substance of the bargain must be examined but even when that is done by reference to the deed of instrument, I see no reason to disagree with the findings of fact which have been expressed by the Appellate Tribunal.

I would, for the reasons which I have given, answer the question of law raised in this reference in the affirmative.

ORMOND, J.—I agree and desire only to add certain remarks. It was contended on behalf of the assessee by Dr. Pal that after the agreement for extension of the lease made in 1933 (printed at page 29 of the Paper Book) there was no right to the Bengal Coal Co., Ltd., to terminate the lease at will. On a perusal of the original lease made in 1916 and the agreement for its extension made in 1933, I am unable to accept this construction of these documents. In my view the term expressed in the last sentence of clause 1 of the lease of 1916, *viz.*, "you shall be at liberty to abandon the lands at any time before the period of the lease expires provided you pay up in full the rents and royalty of every description due to me up to the time of abandonment and no objection will be made to that effect" continued operative in so far as it gave a right to terminate the lease at will and was modified only as to the terms on which such right to terminate were to be exercised. It appears to me therefore that after the agreement of 1933 the position as to the right of the Bengal Coal Co., Ltd., to terminate at will remained and was modified only to this extent: that whereas in 1916 the Bengal Coal Co., Ltd., had a right to terminate at will without payment of any royalties for the balance of coal in the seams left unworked, after 1933 it can only terminate with payment of royalty for the unworked coal.

Dr. Pal pursuing the contention made by him that the Bengal Coal Co., Ltd., after 1933 had no right to terminate the lease at will, relied strongly on such cases as *Mallett* v. *Staveley Coal and Iron Co., Ltd.*[1] and

(1) (1928) 13 Tax Cas. 772.

Van den Berghs, Ltd. v. *Clark*[1]. In *Mallett's case*[2], it will be seen the money was paid by way of consideration or compensation for the surrender of two leases. The one lease (of 1882) contained power to the company to surrender the lease only as to the entirety of the hereditaments demised and did not empower the company to surrender any part or parts of the demised seams as distinct from the entirety of the hereditaments demised, as appears from the report at page 774. In the case of the other lease (of 1919) this contained no power to the company to surrender the whole or any part of the seams before the fulfilment of the period of the lease. The company when entering into the agreement for surrender did not purport to be exercising any right of surrender under the lease of 1882. The payment was thus made by agreement as to the amount for settlement of what, had the parties not agreed, would have given grounds for a claim for damages for wrongful termination of the leases. The payment was held to be capital expenditure to get rid of an onerous liability arising from a permanent asset of the business, and not to be an admissible deduction in calculation of profits for income-tax purposes in the assessment of the party making the payment. In the case of *Van den Berghs Ltd.* v. *Clark* [1] also there was no right given to the company to terminate the agreement before its due date of completion. It was held that the payment received was for surrender of a capital asset and therefore not assessable as profits to income-tax in the hands of the receiving company. It was in those circumstances in those cases that the payments made for compensation for termination of agreements not terminable in themselves before due date were held to be capital payments or capital receipts respectively and not in the nature of revenue.

Taking the view that we take on the documents in the present case that the mining lease was terminable at will in terms of the lease itself, it will be seen that there is an important difference between the present case and the class of cases such as the two above mentioned; where the payment (held to be of a capital nature) was being made as compensation settled in a special agreement for termination of an otherwise non-terminable agreement. In such cases it could well be said, that by the special agreement, there was being effected, on capital account, either in certain cases (as where the party adjudicated on was making the payment), a payment to get rid of an onerous capital liability, or, in other cases, (as where the party adjudicated on was receiving the payment), a receipt as a capital receipt for the sale or surrender of a capital asset; in both instances by the purchase or sale, as the case might be, of the right to terminate, for an agreed amount as compensation, an otherwise non-terminable agreement. Here in the present case the termination of the lease is in accordance with the express terms stated in the lease of 1916 itself read with the subsidiary agreement of

(1) (1934) 19 Tax Cas. 390; 3 I.T.R. Eng. Cas. 17. (2) (1928) 13 Tax Cas. 772.

extension of 1933. The company is thus merely exercising its right of termination of the lease in accordance with express terms in the lease. Under clause 7 it was expressly provided that royalty for unworked coal should be payable in the event of the lease being determined; as I read that clause.

It was argued on behalf of the assessee that clause 7 referred only to a position when the lease was continuing. Though this might well be the natural meaning of the words, were royalties made payable only in the event of the coal being "rendered inaccessible," it cannot, in my view, be the meaning to be attributed to the other circumstances contemplated by the clause when coal should have been "abandoned." It is true that when the lease was continuing, and the working of the colliery by the Bengal Coal Co., Ltd., was continuing, it might have been open to the company to make a definite expression of a decision in advance saying that "it had abandoned certain coal." In that event royalty would no doubt have become then payable even before completion of working. There is, in this case, however no question of any abandonment by express declaration; and the clause, as I read it, must necessarily cover abandonment also when the lease is determined and where there is no express declaration of abandonment.

In the present case therefore, since the contract was terminated as provided for in the contract itself and in accordance with the terms of the contract, it thus becomes unnecessary to look outside the contract in order to ascertain the nature of the payment of one lakh of rupees made.

I find this money was paid directly under clause 7. It is of course immaterial that the amount paid was agreed in a round sum as monies such as were payable under clause 7. This sum of one lakh of rupees which was an agreed amount to be paid for the dues under clause 7 was, in my view, therefore, clearly a payment of royalties.

In this view of the matter it is unnecessary further to consider cases such as those of *Mallett* v. *Staveley Coal and Iron Co., Ltd.* [1], and *Van den Berghs, Ltd.* v. *Clark* [2], mainly relied on by Dr. Pal. I do not, however, wish to be taken to say that even if the payment had here been made not directly under the contract but as compensation fixed by special agreement for what would but for the special agreement have been its wrongful termination, it could not also, in the circumstances of the present case, have been held still to be income and not capital.

As was observed by Lord Macmillan in the case of *Van den Berghs Ltd.* v. *Clark* [2] at page 429 :—

"The reported cases fall into two categories, those in which the subject is found claiming that an item of receipt ought not to be included in

(1) (1928) 13 Tax Cas. 772. (2) (1934) 19 Tax Cas. 390 ; 3 I.T.R. Eng. Cas. 17.

computing his profits and those in which the subject is found claiming that an item of disbursement ought to be included among the admissible deductions in computing his profits. In the former case the Crown is found maintaining that the item is an item of income ; in the latter, that it is a capital item. Consequently the argumentative position alternates according as it is an item of receipt or an item of disbursement that is in question and the taxpayer and the Crown are found alternately arguing for the restriction or the expansion of the conception of income."

Various cases on both sides are then considered in that judgment. I need only for the present purpose refer as an illustration to the case of *Anglo-Persian Oil Co., Ltd.* v. *Dale* [1]. That was a case where there was an agreement between the Anglo-Persian Oil Co., Ltd., and another company to act as an agent of the former. The agreement was made for 10 years and remuneration was fixed on the basis of commission on business done. There was in that case, just as in the case of *Mallett* v. *Staveley Coal and Iron Co., Ltd.* [2], and in the case of *Van den Berghs, Ltd.* v. *Clark* [3], no right to terminate the agreement before due time. The agreement was for ten years. The Anglo-Persian Oil Co., Ltd., having decided that, as a matter of business, it would be preferable to terminate the agreement of agency, entered into a separate agreement with the other company by which the agency was terminated. In consideration for this, the Anglo-Persian Oil Co., Ltd., was to pay and did, in fact, pay a sum of £3,00,000. It was finally decided in that case that this sum was not capital but a payment in the nature of a revenue payment, and in the accounts of the company making the payment an admissible deduction in calculation of profits —the basis of the decision, as I understand it, being that had the agreement of agency continued, the agent company would have been entitled to commission yearly. As the parties had agreed to terminate the agency agreement the lump sum paid was, to look at the matter in substance, commission or in lieu of commission, and as such was not a payment of a capital nature.

It is true that in that case the matter was being considered from the point of view of the liability to tax of the party making the payment, whereas in the present case the matter is to be considered before us from the point of view of the liability to tax of the party receiving payment. But in the present case if it is correct to decide that in so far as the payment was made by the Bengal Coal Co., Ltd., this was for royalties, in my view it must equally be decided that that sum of one lakh of rupees was received by the assessee as royalty. While it is unnecessary, in the view that we take of the document in this case, to consider what would have been the position had there been no right for the Bengal Coal Co., Ltd., to terminate the lease at will, I have referred to this single case as a

(1) (1931) 16 Tax Cas. 253.
(2) (1928) 13 Tax Cas. 772.
(3) (1934) 19 Tax Cas. 390 ; 3 I.T.R. Eng. Cas. 17.

mere illustration to show that it would not conclusively follow, simply because the payment was made in consideration of terminating a lease not terminable but for mutual special agreement at the time when it was being terminated, that therefore it should necessarily be held that the payment was of a capital nature.

In regard to the contention of Dr. Pal for the assessee that this was a casual receipt under Section 4 (3) (vii) of the Income-tax Act, on the facts in my view it is not. This payment was expressly provided for in the lease and therefore it was foreseen, known, anticipated and provided for as it was put by Dr. Gupta. It has its source in the agreement itself where it is clothed with the nature of royalty. In these circumstances it cannot be held to be a casual receipt.

For these reasons besides those expressed by my learned brother I agree that the answer to the question referred to us should be in the affirmative.

Reference answered in the affirmative.

[IN THE CHIEF COURT OF SIND.]

COMMISSIONER OF INCOME-TAX, BOMBAY

v.

LARKANA JACOBABAD (SIND) LIGHT RAILWAY LTD.

TYABJI and O'SULLIVAN, JJ.

May 22, 1945.

INDIAN INCOME-TAX ACT (XI OF 1922), SEC. 25 (3), (4)—INDIAN INCOME-TAX ACT, 1918—COMPANY—RAILWAY COMPANY—INVESTMENT OF UNEXPENDED CAPITAL IN SECURITIES PENDING CONSTRUCTION OF RAILWAY LINES—WHETHER COMPANY CARRIES ON BUSINESS—SCOPE OF SEC. 25 (4)—"INTEREST ON SECURITIES" OF COMPANY ALONE ASSESSED UNDER ACT OF 1918—SUCCESSION IN 1939—WHETHER COMPANY ENTITLED TO BENEFIT OF SEC. 25 (4).

The meaning of the expression "carrying on a business" for the purpose of the Income-tax Act is not affected by the question whether the assessee is an individual or a company.

An assessee who was not charged to tax under the head "Business" or "Professional earnings" under the provisions of the Indian Income-tax Act, 1918, cannot claim the relief provided for under Section 25 (4) of the Indian Income-tax Act, 1922.

A company which was formed for the purposes of making a profit from a business and which had only been charged to tax under the head "interest on securities" under the Act of 1918, cannot, merely by reason of its being a company, be regarded as having been charged to tax on its business.

The assessee was a company incorporated under the Indian Companies Act, 1913, in February 1916, in pursuance of a concession secured from the

Secretary of State for India for the purpose of constructing, maintaining and carrying on a railway in the Province of Sind. Under the memorandum of association the company was authorised to invest in securities moneys not immediately required. Since the whole of the share capital of the company was not immediately required for expenditure on the construction of the railway line, the company invested, in accordance with an agreement made between it and the Secretary of State, substantial sums in Government of India loans, bonds and treasury bills and received income from the interest on these investments. The railway line was completed and was opened for traffic only in February 1922. During the years 1918-19, 1919-20, 1920-21 and 1921-22 the company was assessed to income-tax under the Income-tax Act, 1918, on the amount of interest realised on Government and other securities. During this period the company did not derive any profit from the working of the railway and no tax was therefore charged under the Act of 1918 on the business of the company. The railway line was taken over by the Secretary of State from 3rd May 1939. In its assessment for 1939-40, the company claimed under Section 25 of the Income-tax Act, 1922, that it should be allowed to substitute the income of the broken period from 1st April 1939 to 2nd May 1939 for the income of the financial year ending on the 31st of March 1939:

Held, *that as no tax was charged on the business of the company under the Act of 1918, it was not entitled to the benefit of sub-section (3) or sub-section (4) of Section 25 of the Act of 1922.*

Cases referred to:—

Birmingham and District Cattle By.-Products Co., Ltd. *v.* Commissioners of Inland Revenue [1919] (12 Tax Cas. 92).

Commercial Properties Ltd., *In re* [1928] (113 I.C. 848; 55 Cal. 1057; 32 C.W.N. 413; 3 I.T.C. 23).

Commissioner of Income-tax, U. P. *v.* Basant Rai Takhat Singh [1933] (60 I.A. 307; 55 All. 452; 144 I.C. 344; A.I.R. 1933 P.C. 180; 6 I.T.C. 459; 1 I.T.R. 197).

Commissioner of Income-tax, Madras *v.* B. J. Fletcher [1935] (3 I.T.R. 223; A.I.R. 1935 Mad. 953; 1935 M.W.N. 749; 69 M.L.J. 611; 158 I.C. 895; 8 I.T.C. 320).

Commissioner of Income-tax, Madras *v.* Mangalagiri Sri Umamaheswara Gin and Rice Factory Ltd. [1926] (52 M.L.J. 360; A.I.R. 1926 Mad. 1032; 2 I.T.C. 251).

Commissioner of Income-tax, Bombay *v.* National Mutual Association of Australasia Ltd. [1933] (1 I.T.R. 350; 57 Bom. 519; 35 Bom. L.R. 896; A.I.R. 1933 Bom. 427; 6 I.T.C. 426).

Commissioner of Income-tax *v.* Shaw Wallace and Co. [1932] (59 I.A. 206; 136 I.C. 742; 34 Bom. L.R. 1033; A.I.R. 1932 P.C. 138; 6 I.T.C. 178).

Commissioners of Inland Revenue *v.* Korean Syndicate Ltd. ([1921] 3 K.B. 258; 90 L.J.K.B. 1153; 125 L.T. 615; 37 T.L.R. 735; 12 Tax Cas. 181).

Fry *v.* Salisbury House Estate Ltd. ([1930] A.C. 432; 99 L.J.K.B. 403; 143 L.T. 77; 46 T.L.R. 336; 15 Tax Cas. 266).

Kaladan Suratee Bazaar Co., Ltd., [1920] (56 I.C. 914; 1 I.T.C. 50).

Liverpool and London and Globe Insurance Company *v.* Bennett ([1913] A.C. 610; 82 L.J.K.B. 1221; 109 L.T. 483; 29 T.L.R. 787; 6 Tax Cas. 327).

Patiala State Bank, *In re* [1941] (9 I.T.R. 95; I.L.R. 1941 Bom. 391; 194 I.C. 712; 43 Bom. L.R. 84; A.I.R. 1941 Bom. 93).

Revell v. Edinburgh Life Insurance Company [1906] (5 Tax Cas. 221).

Sadhucharan Roy Chowdhri, *In re* [1935] (3 I.T.R. 114; 62 Cal. 804; A.I.R. 1935 Cal. 344; 39 C.W.N. 739; 156 I.C. 394; 8 I.T.C. 177).

Sind Light Railway Co. Ltd. v. Commissioner of Income-tax, Bombay [1932] (6 I.T.C. 271).

Smith v. Anderson [1880] (15 Ch. D. 247; 50 L.J. Ch. 39; 43 L.T. 329; 29 W.R. 21).

South Behar Railway Co. Ltd. v. Commissioners of Inland Revenue ([1925] A.C. 476; 94 L.J.K.B. 386; 132 L.T. 802; 41 T.L.R. 328; 12 Tax Cas. 657).

Reference under Section 66 (2) of the Indian Income-tax Act (XI of 1922) by the Commissioner of Income-tax, Bombay, Sind and Baluchistan: Reference No. 31 of 1943.

The Statement of Case and the opinion of the Commissioner are fully set out in the judgment.

Partabrai D. Punwani, for the Commissioner.

Hakumatrai M. Idnani, for the assessee.

JUDGMENT.

TYABJI, J.—This is a reference by the Commissioner of Income-tax, Bombay, Sind, Baluchistan and Ajmer-Merwara, under Section 66 (2) of the Indian Income-tax Act (XI of 1922) (hereinafter called the Act), made at the instance of the Larkana Jacobabad (Sind) Light Railway Co., Ltd., (hereinafter called the company) in respect of an assessment for the year 1939-40. The company claims to be entitled to the benefit of relief under sub-clause (3) or (4) of Section 25 of the Act, a claim which has not been allowed by the Income-tax Commissioner. The facts have been stated in the reference as follows:—

" The company was incorporated under the Indian Companies Act, VII of 1913, on the 10th of February 1916, in pursuance of a concession secured by Messrs. Forbes, Forbes, Campbell & Co., Ltd., who are the managing agents of the company, from the Secretary of State for India in Council. The primary purpose of the company, as stated in clause (1) of Article III of the memorandum of association, was 'to survey, construct, complete and make ready for public traffic and to maintain, develop, work, manage and carry on a line of railway or tramway of an approximate length of 75 miles starting from Larkana in the Sind Province, and proceeding thence to Jacobabad *via* Kambar and Shahdadkote.'.........The authorised capital of the company was Rs. 30 lakhs, of which Rs. 27 lakhs were actually issued, this being the amount of capital which the company had undertaken to provide in the first instance for the construction of the railway. The line was completed and was opened for traffic in February 1922.

2. The exact terms of the agreement with the Secretary of State were under discussion for some years and the agreement was actually signed on the 5th of February 1924.........In accordance with the agreement the line was handed over on completion to be maintained by the Secretary of

State through the agency of the North Western Railway. Under the provisions of Schedule II the profits earned on the working of the line were to be divided between the company and the Secretary of State, subject to the proviso that if in any year the company's share of the earnings was not sufficient to pay the shareholders a return of 5% per annum on their investments the Secretary of State would relinquish his share to the extent required to make up that percentage. The Secretary of State also reserved to himself the option of taking over the line at any time on certain conditions. This option was actually exercised on the 2nd of May 1939 and the company then went into liquidation.

3. Clause (21) of Article III of the memorandum of association states that one of the objects of the company is 'generally to lend, invest and deal with the moneys of the company not immediately required upon such securities or without security and in such manner as may from time to time be determined.' A similar provision exists in clause (25) of Article III of the memorandum of association and in clause II of Article 129 of the articles of association. Any action taken by the company in pursuance of these provisions was however governed by clause 22 of the agreement with the Secretary of State which reads as follows:—

'Unexpended capital balances in the hands of the company in any Treasury or Treasuries shall from time to time, if the Secretary of State determines, be invested or deposited at interest in the name of the company in such manner as the Secretary of State may from time to time prescribe, and no such investment or deposit shall be made by the company without the prior approval in writing of the Secretary of State nor shall any investment or deposit so made be realised, called in or re-invested by the company unless with such approval. Any loss incurred from such investments shall be charged to the capital account of the company.'

4. Since the whole of the share capital of the company was not immediately required for expenditure on the construction of the line substantial sums were in fact invested in Government of India loans, bonds and treasury bills, and the company received income from the interest on these investments. This income was used for the purpose of paying interest to the shareholders at the rate of 4% in accordance with clause (26) of Article III of the memorandum of association. The company did not however draw up any profit and loss account or declare any dividends in the years prior to the opening of the line.

5. The company was assessed to income-tax under the Indian Income-tax Act of 1918 for the years 1918-19, 1919-20, 1920-21 and 1921-22, but these assessments related only to income from interest. There is a note below the assessment order for 1919-20 which states that 'the company is not liable to E. P. D. Act (Excess Profits Duty) since the above income is

from investments and not from business, *i.e.*, the railway has not yet commenced working.'

6. The relevant entries in the return submitted by the company for the income-tax year 1921-22 were as follows:—

'Profits as per accounts submitted nil. Amount of interest realised on Government and other securities and accounted for in the account Rs. 92,918-15-0.'

The income-tax assessment was made on the basis of this return, allowance being given for interest on tax-free loans which amounted to Rs. 49,607 and for expenses amounting to Rs. 13,015. This was the last assessment made under the Income-tax Act of 1918 since the present Act came into force on the 1st of April 1922.

7. As has already been stated the line was taken over by the Secretary of State with effect from the 3rd of May 1939. In connection with its assessment for 1939-40 the company claimed that it should be allowed to substitute the income of the broken period from the 1st of April 1939 to the 2nd of May 1939 for the income of the financial year ending on the 31st of March 1939 under the provisions of sub-sections (3) and (4) of Section 25. These sub-sections read as follows:—

'(3) Where any business, profession or vocation on which tax was at any time charged under the provisions of the Indian Income-tax Act, 1918, is discontinued, then, unless there has been a succession by virtue of which the provisions of sub-section (4) have been rendered applicable, no tax shall be payable in respect of the income, profits and gains of the period between the end of the previous year and the date of such discontinuance, and the assessee may further claim that the income, profits and gains of the previous year shall be deemed to have been the income, profits and gains of the said period. Where any such claim is made, an assessment shall be made on the basis of the income, profits and gains of the said period, and if an amount of tax has already been paid in respect of the income, profits and gains of the previous year exceeding the amount payable on the basis of such assessment, a refund shall be given of the difference.

(4) Where the person who was at the commencement of the Indian Income-tax (Amendment) Act, 1939, carrying on any business, profession or vocation on which tax was at any time charged under the provisions of the Indian Income-tax Act, 1918, is succeeded in such capacity by another person, the change not being merely a change in the constitution of a partnership, no tax shall be payable by the first mentioned person in respect of the income, profits and gains of the period between the end of the previous year and the date of such succession, and such person may further claim that the income, profits and gains of the previous year shall be deemed

to have been been the income, profits and gains of the said period. Where any such claim is made, an assessment shall be made on the basis of the income, profits and gains of the said period, and, if an amount of tax has already been paid in respect of the income, profits and gains of the previous year exceeding the amount payable on the basis of such assessment, a refund shall be given of the difference.'

The question whether sub-section (3) or sub-section (4) would be the more appropriate to the present case does not appear to be free from doubt. This would depend on whether the Secretary of State can be held to have succeeded to the business carried on by the company or whether the business should be regarded as having been discontinued. It is not necessary to reach a decision on this question since the procedure prescribed by the Act is the same in each case, but it may be mentioned that in the case of *Sind Light Railway Co., Ltd.* [1], it was held that the Government had succeeded to the business of the acquired railway within the meaning of Section 26 (2) of the Act as it stood before the amendments made in 1939.

8. The Income-tax Officer, B Division, Karachi, who dealt with the assessment came to the conclusion that the company was not entitled to relief under either of these sub-sections since no tax had been charged on the business of the company under the provisions of the Income-tax Act of 1918. He accordingly assessed the company to income-tax and super-tax on the assessable income of the accounting period ending on the 31st of March 1939, which amounted to Rs. 1,47,934...........

9. The company then appealed to the Assistant Commissioner of Income-tax, Sind and Baluchistan, who agreed with the finding of the Income-tax Officer and confirmed the assessment...........

10. Thereafter the company submitted an application under Sections 33 and 66 (2) of the Act in which they requested the Commissioner of Income-tax either to exercise his powers of revision or to make a reference to the Chief Court...... Since I find myself in agreement with the Assistant Commissioner's decision I am unable to revise the assessment, but the company is entitled to a reference on any question of law which arises from the appellate order."

The questions which arise and the opinion of the Commissioner are then stated as follows :—

"*Questions for decision*—In its application the company has formulated four questions, but it seems to me that there are in reality only two questions which require consideration. These questions might be stated as follows :—

(1) Whether in the circumstances of the case the company is entitled to receive the benefit of sub-section (3) or sub-section (4) of Section 25 of the Act.

(1) (1932) 6 I.T.C. 271.

(2) If the answer to the first question is in the affirmative, whether the relief is due only in respect of the income from the business of investments which was taxed under the Act of 1918 or also in respect of profits of the business of working the railway line which were not taxed under that Act.

I accordingly refer these questions for the decision of the Chief Court.

Opinion of the Commissioner.—In support of its claim the company has quoted a number of English decisions. Apart from the fact that these cases are not entirely relevant or of much assistance for the consideration of the question involved in this case, their Lordships of the Privy Council in *Shah Wallace's case* [1] deprecated the practice of relying on English income-tax decisions for the purpose of construing the Indian Income-tax Act which was not *in pari materia* with the English Act. If any guidance is to be sought from English cases regarding the questions in issue here, then by parity of reasoning the conclusion would be that the different sources of income specified in Section 6 of the Indian Act are mutually exclusive, as are the different Schedules under the English law to which these heads are comparable. In *Fry* v. *Salisbury House Estate Ltd.*[2], Lord Atkin said:—

'The option of the revenue authorities to assess under whichever Schedule they prefer in my opinion does not exist and is inconsistent with the provisions of the Income Tax Acts throughout their history .... My Lords, nothing could be clearer to indicate that the Schedules are mutually exclusive ..... Similarly I am of opinion that income derived by a trading company from investments of its funds, whether temporary or permanent, in Government securities must be taxed under Schedule 'C', and cannot for purposes of assessment under Schedule 'D' be brought into account.'

The only option that exists is to tax income from investments either under Case I or Case IV of Schedule 'D' (vide *Revell* v. *Edinburgh Life Assurance Co.*[3]). It is important to note that the option available is only an option to choose between cases of the same Schedule.

Section 6 of the Indian Income-tax Act reads as follows:—

'Save as otherwise provided by this Act the following heads of income, profits and gains shall be chargeable to income-tax in the manner hereinafter appearing, namely:—

(1) Salaries.

(2) Interest on securities.

(3) Income from property.

(4) Profits and gains of business, profession or vocation.

(5) Income from other sources.'

(1) (1932) 6 I.T.C. 178, at p. 180.
(2) (1930) 15 Tax Cas. 266.
(3) (1906) 5 Tax Cas. 221.

As regards the opening words of the section, it may be stated at the outset that the only exception is the one mentioned in Section 10 (7) which lays down that 'notwithstanding anything to the contrary contained in Section 8, 9, 10, 12 or 18, the profits and gains of any business of insurance and the tax payable thereon shall be computed in accordance with the rules contained in the Schedule to this Act.' The classification of the different heads of income under Section 6 of the Act of 1922 is practically the same as in Section 5 of the Act of 1918 except that in the latter ' business ' and ' profession ' were shown under separate categories. The scheme of the Act is that the various heads of income enumerated in Section 6 are assessable in the manner laid down in Sections 7 to 12 in respect of each head even although the income under various heads is received by one and the same assessee. This is clear from Section 24 (1) which says that ' where any assessee sustains a loss of profits or gains in any year under any of the heads mentioned in Section 6, he shall be entitled to have the amount of the loss set off against his income, profits or gains under any other head in that year.'

If an income appropriately falls under one head, it cannot be assessed by the Income-tax Officer under another. In *Basant Rai Takhat Singh*[1], Lord Tomlin said: ' It is to be noted that Section 12 does not come into operation until the preceding heads are excluded.' Before an income can fall under the head ' business ' specified in Section 6, it must satisfy the definition of the word ' business ' which was the same in the Act of 1918 as in the Act of 1922. Since the income of the assessee from interest on securities, treasury bills etc., fell under Sections 8 and 12, it could not be assessed under the head ' business ' which is chargeable under Section 10. The fact that certain expenses which might not have been admissible under these heads were allowed is not sufficient to establish that the income was assessed or did fall under the head ' business.'

Sub-sections (3) and (4) of Section 25 refer to ' any business, profession or vocation on which tax was at any time charged under the provisions of the Indian Income-tax Act, 1918.' It is only the income appropriately falling under 'business, profession or vocation' and assessable under Section 10 which is eligible for the benefit of these sub-sections. In the present case it is admitted that the assessments made under the Act of 1918 were made only on the income from interest and not on income derived from the working of the railway. The company argues that the investing of its surplus funds formed part of its business and points out that under clauses (21) and (25) of its memorandum of association one of the objects with which it was established was ' to lend, invest and deal with moneys of the company not immediately required.' It does not necessarily follow however that all the activities which a company is authorised to undertake

(1) [1933] 1 I.T.R. 197.

can be treated as part of its business for income-tax purposes. Most companies, whatever their principal activity may be, are authorised to acquire property and to let it out on rent, but the rental income received from persons not connected with the business of the company is clearly assessable under Section 9 and not under Section 10 of the Act. Similarly if a company invests its surplus funds in Government securities the interest received from the securities is assessable under Section 8 which specifically deals with this source of income.

It is true that there are companies whose sole or main business consists in holding and dealing securities but the present company is not a company of that type. The funds which were invested consisted only of the surplus share capital and not of money earned through business activities, and all such investments required the sanction of the Secretary of State under clause 22 of the agreement. The obvious purpose of this provision was to ensure that the capital of the company would remain available for the construction of the line and would not be used for other business or speculative transactions. Clause 22 of the agreement further provides that any loss incurred through the investments should be charged to the capital account of the company and neither profit nor loss on the sale of securities was ever taken into consideration for income-tax purposes. The company did not itself treat the income from its investments as business income. As has already been stated it did not draw up a profit and loss account or declare a dividend until after the line had been opened for traffic. It did not declare the income for investments under 'profits' in its income-tax returns and it was exempted from excess profits duty on the ground that it was not doing business.

In these circumstances it seems to me that the income which was taxed under the Act of 1918 has been rightly held to be income which would be assessable not under Section 10 but under other sections of the present Act, and that it is not income from a 'business, profession or vocation' for the purpose of sub-sections (3) and (4) of Section 25. I therefore respectfully submit that the first question should be answered in the negative.

If my opinion on the first question is accepted the second question will not arise. If, however, it should be held that the income from interest on Government or other securities and investments fell under the head 'business' and was assessed as such under the Act of 1918, I would submit that it was a distinct and separable business from that of the working of the railway line run on a profit-sharing basis. The question whether a business is separate is a finding of fact. Although, speaking generally, it may be said that a company can have only one business as set out in the memorandum and articles, the revenue decisions, particularly in excess profits duty cases and cases of discontinuance and succession, proceed on the basis

that for the purposes of the taxing Acts a company may have more than one separable business. Even for the purpose of setting off a business loss carried forward to a succeeding year Section 24 (2) allows a 'set-off against the profits and gains, if any, of the assessee from the same business.' In my respectful opinion therefore if any relief is at all due on the ground that the income assessed under the Act of 1918 was from business, the company would be entitled to relief only to a limited extent, *i.e.*, it might claim to substitute only the income from investments for the period from the 1st of April to the 2nd of May 1939 for the income from that business of the 'previous year.' I would submit that the second question should be answered accordingly."

It was assumed by both parties before us during the argument that the Secretary of State had succeeded to the business of the company in May, 1939, and the main question, it was admitted, was, "whether the company was at the commencement of the Indian Income-tax (Amendment Act) carrying on any business on which tax was at any time charged under the provisions of the Indian Income-tax Act, 1918."

After hearing lengthy arguments on both sides we have no doubt that the Commissioner was right in answering the question in the negative. The company completed the construction of the railway and the other preparations for running the railway on the 16th February 1922, when the railway first commenced to function. This date falls within the period 1-4-1921 to 31-3-1922 in respect of which the last assessment was made under the provisions of the Act of 1918. The profit on the business of the company shown for this period—which included the period 16-2-1922 to 31-3-1922 during which the railway was actually worked—was nil, and thus no tax was in fact charged on the business carried on by the company under the provisions of the Act of 1918.

We have heard a very elaborate argument about the meaning of the word "business," of its wider and narrower significations, and a number of decisions have been discussed before us, including *Smith* v. *Anderson*[1]; *Liverpool and London and Globe Insurance Company* v. *Bennett*[2]; *Commissioners of Inland Revenue* v. *Korean Syndicate Ltd.*[3]; *South Behar Railway Co., Ltd.* v. *Commissioners of Inland Revenue*[4]; *Commissioner of Income-tax, Madras* v. *Mangalagiri Sri Umamaheswara Gin and Rice Factory Ltd., Guntur and Another*[5]; *Commissioner of Income-tax, Bombay Presidency and Aden* v. *National Mutual Association of Australasia Ltd.*[6], and *In re The Patiala State Bank*[7]. It was argued that all the activities of the company from the date of its inception in 1916, including the investment of

(1) (1880) 15 Ch. D. 247, at p. 260.
(2) [1913] A.C. 610, at p. 615.
(3) [1921] 3 K.B. 258, at pp. 273, 275.
(4) [1925] A.C. 476.
(5) (1926) 51 M.L.J. 360.
(6) (1933) 57 Bom. 519, at p. 528; 1 I.T.R. 350.
(7) [1941] 9 I.T.R. 95; 43 Bom. L.R. 84.

its funds and the collection of interest thereon, were part of the business for which the company was formed, and that ultimately every part of the income of the company, no matter from what source it was derived, would affect the company's profits, if not in the years when the income was received, at least in later years. Of this of course there can be no doubt. When it was further argued that the tax paid by the company on its income from its investments under the head "interest realized on Government and other securities" was therefore a tax charged on the business of the company, because the company was, at the time, engaged in doing what was its business, it appears to us that the argument is clearly vitiated by the fact that it omits to take into account the words "charged under the provisions of the Income-tax Act of 1918." The question must of course be considered in the light of the scheme under which tax is charged under the Act. It does not help the company to point out that it was not, for instance, a sporting or a charitable concern, but a company formed for the purpose of running a business for profit, when the question is whether its business had or had not in fact been charged as a business under the provisions of the Act of 1918, so as to bring the company's case within the language of sub-clause (4) of Section 25. A fact which is much more to the point is that the actual business of the company, from which alone it was possible for it to make the profit for which it was formed, did not commence until the railway started to work on the 16th February 1922. It was only then that it commenced the business on the profit of which income-tax could be charged under the provisions of the Act. In the *Birmingham and District Cattle By-Products Co., Ltd.* v. *Commissioners of Inland Revenue* [1], the company was formed on the 20th June 1913, and the period up to October 1913, when manufacture was actually commenced, was spent in purchasing and erecting the machinery and plant and making other preparations. Rowlatt, J., held that the Commissioners had rightly held that the business of the company had not for taxation purposes commenced until October 1913.

It has been repeatedly pointed out that the meaning of the expression "carrying on a business" for the purposes of this Act is not affected by the question whether the assessee was an individual or a company. In *In re Kaladan Suratee Bazaar Co., Ltd.* [2], it was held that where a company held house property and distributed the rents therefrom in the form of dividends to its shareholders it was not carrying on a "business" within the meaning of the Act, any more than when an individual did what the company was doing. In *In re Commercial Properties Ltd.*[3], Rankin, C.J., said :—

"In my judgment, the words of Section 6 and Section 9 and Section 10 must be read so as to give some effect to the contrast that is there made

(1) (1919) 12 Tax Cas. 92.
(2) (1920) 56 I.C. 914.
(3) (1928) I.L.R. 55 Cal. 1057.

between income, profits and gains from 'Property' and from 'Business,' and I entirely refuse my assent to the proposition that because it happens that the owner of a property is a company which has been incorporated for the purpose of owning such property, therefore, the income derived from 'property' must be regarded as income derived from 'business.' In my judgment, income derived from 'property' is a more specific category applicable to the present case" and

"In my judgment, these cases are not authorities to the effect that as between the word 'Property' and the word 'Business' in Section 6 of the Indian Income-tax Act, 1922, a case of this character is to be put under the word 'Business.' It comes more directly and specifically under the word 'Property.' In my judgment, the mere fact that the house-owner is a company does not change the incidence of the tax in the way contended for."

In *In re Sadhucharan Roy Chowdhri*[1], the question was whether the letting of a jute press was or was not the carrying on of a business, and it was stated (by Lort-Williams and Jack, JJ.) :—

"that the lessor in that case was a registered company seems to me to be irrelevant."

The case which is most in point on the question before us is *Commissioner of Income-tax, Madras* v. *B. J. Fletcher*[2]. One of the questions in this case was whether the assessee Fletcher, who had been taxed under the head "Salaries" under the Act of 1918, and who claimed to have pursued a "vocation" during that period, could on a discontinuance claim the bénefit of sub-clause (3) of Section 25. Beasley, C.J., stated in this connection :—

"I am clearly of the view that this question must be answered in the negative. The assessee's contention is that he has received this amount by reason of the vocation carried on by him. The answer to this contention is that he has been assessed under the head of 'salary' under Section 7 (1) of the Act. Section 6 provides that:

'The following heads of income, profits and gains shall be chargeable to income-tax in the manner hereinafter appearing, namely :—(i) Salaries, (ii) Interest on securities, (iii) Property, (iv) Business, (v) Professional earnings and (vi) Other sources.'

Each of these is dealt with in separate sections of the Act. The assessee has always been assessed under Section 7 (1). This income clearly does not fall under any of the clauses (ii), (iii), (iv), (v) and (vi). Section 25 (3) was intended to prevent a double assessment. It cannot be intended to apply to a case where income-tax is assessed on salaries in the year in which they are earned. If the section were to apply, it would lead to this very strange and unreasonable result that an assessee who chooses to relinquish his appointment in the eleventh month of the year would escape payment of

(1) (1935) I.L.R. 62 Cal. 804 ; 3 I.T.R. 114. (2) (1935) 69 M.L.J. 611 ; 3 I.T.R. 223.

income-tax on the salary earned by him in these eleven months whereas, if he continued for one month longer, admittedly he would be assessable on his salary in the whole of the twelve months. Mr. T. M. Krishnaswami Ayyar was quite unable to give any reason why such should be the result. In my view, therefore, as this sum falls to be assessed under Section 7 (1) of the Act, Section 25 (3) cannot be applied to it."

It appears to us to be clear that an assessee who was not charged under the head "Business" or "Professional earnings" under the provisions of the Act of 1918, cannot claim the relief provided for under clause (4) of Section 25 of the Act; and that the contention that a company, formed for the purposes of making a profit from a business, which had only been charged under the head "Interest on securities" under the Act of 1918, was, merely by reason of its being a company, to be regarded as having been charged on its business cannot be accepted.

The company will bear the costs of this reference.

Reference answered accordingy.

[IN THE CHIEF COURT OF SIND.]

COMMISSIONER OF INCOME-TAX, BOMBAY
v.
VALIRAM BHERUMAL.

DAVIS, C. J., and THADANI, J. January 10, 1945.

INDIAN INCOME-TAX ACT (XI OF 1922 AS AMENDED IN 1939), SECS. 4 (1) PROVISO (3), 16 (1)—FOREIGN INCOME—REGISTERED FIRM—REBATE OF RS. 4,500—WHETHER CAN BE ALLOWED ON TOTAL INCOME OF FIRM AND SHARE OF INCOME OF EACH PARTNER.

When the income of a registered firm has had the benefit of the rebate of Rs. 4,500 under the third proviso to Section 4 (1) of the Indian Income-tax Act, 1922, the benefit of that rebate cannot again be claimed by each individual partner upon his share in the profts which is liable to taxation.

Section 4 (1) proviso deals with the assessment of the tax and Section 16 (1) deals with the levy. The rebate is allowed when the income-tax is assessed, it is not allowed again upon the levy.

Cases referred to:—

Babu Raman Lal Kondai, *In re* [1943] (11 I.T.R. 263).

Mohanlal Hiralal *v.* Commissioner of Income-tax, C.P. and U.P. [1943] (11 I.T.R. 259).

Reference under Section 66 (2) of the Indian Income-tax Act (XI of 1922) by the Commissioner of Income-tax, Bombay: Reference No. 50 of 1942.

JUDGMENT.

DAVIS, C. J.—This is a reference by the Commissioner of Income-tax at the request of one Bherumal Ghanomal, who is a partner in the firm of Messrs. Bherumal Ghanomal, doing business in Java and Japan.

There are two questions referred to us :—

1. Whether in the circumstances of the case, the assessee has been rightly assessed on his accrued income from the registered firm, and

2. Whether the assessee is entitled under the third proviso to Section 4 (1) of the Act, to deduct a sum of Rs. 4,500 from his share of that income.

The difference in the two incomes assessable to tax as put forward by the assessee and the learned Commissioner is considerable, because the assessee contends that he is liable to be taxed only on the foreign income remitted to India which is Rs. 42,252, while the learned Commissioner claims that he is liable to be taxed upon his share in the profits of the firm, which amounts to Rs. 91,023. As the learned Commissioner, however, points out the question as to whether the firm is resident or not is not now open to argument; this is a question of fact. The finding of the learned Commissioner was disputed in a previous application to this Court; it was summarily dismissed; and Mr. Kimatrai now admits that he cannot be heard to argue on the question as to whether this firm is registered and whether the assessee is not liable to be assessed upon his accrued income as distinct from his remitted income.

On the second question Mr. Kimatrai finds his arguments made somewhat difficult by two judgments, one of the Calcutta High Court in the reference under Section 66 (2) of the Income-tax Act (XI of 1922) in the matter of *Babu Raman Lal Kondai*[1], which is referred to with approval and followed by the Nagpur High Court in the case of *Mohanlal Hiralal v. Commissioner of Income-tax, C. P. and U. P.*, reported in Income-tax Reports 1943, page 259. Briefly the assessee claims that he is entitled to a double rebate of Rs. 4,500, a rebate on the income of the firm as a whole and a rebate on the income of each individual partner. If this was so, incomes liable to taxation might easily disappear, the twenty partners of a firm for instance would each claim the benefit of the rebate of Rs. 4,500. The simple truth appears to be that a partner in the firm is not entitled to a double rebate of Rs. 4,500 and that when the income of the registered firm has had the benefit of the rebate, then the benefit of that rebate cannot again be claimed by each individual partner upon his share in the profits which is liable to taxation.

Section 4 (1) proviso, in short, deals with the assessment of the tax and Section 16 (1) deals with the levy. These two sections in their separate

(1) [1943] 11 I.T.R. 263.

functions should not be confused. The rebate, in short, is allowed when the income-tax is assessed : it is not allowed again upon the levy.

The answer, then, to the second question referred to us by the Income-tax Commissioner is in the negative. The first question does not, as we have explained, arise. The Income-tax Commissioner is entitled to his costs. *Reference answered accordingly.*

[IN THE CALCUTTA HIGH COURT.]

BALLYGUNGE BANK LTD., CALCUTTA

v.

COMMISSIONER OF INCOME-TAX, BENGAL.

GENTLE and ORMOND, JJ. April 12, 1946.

INDIAN INCOME-TAX ACT (XI OF 1922), SECS. 9, 10—COMPANY—INCOME DERIVED FROM OWNERSHIP OF BUILDINGS—WHETHER ASSESSABLE UNDER SEC. 9 OR 10—COMPANY OBTAINING LEASE OF PROPERTY ON CONDITION THAT HOUSES CONSTRUCTED WOULD BELONG TO LESSORS AFTER EXPIRY OF TERM—RENTS DERIVED FROM BUILDINGS—WHETHER ASSESSABLE UNDER SEC. 9.

Income derived from the ownership of buildings is chargeable to tax under Section 9 of the Indian Income-tax Act irrespective of whether an individual or a company is the owner and also irrespective of whether one of a company's objects, or its sole object, is to acquire and let out buildings at rents ; ownership itself is the criterion of assessment under that section.

The assessees, a limited company, which had as one of their objects to acquire land, build houses and let them to tenants, obtained a lease of a plot of land for a period of 40 years. The lease deed provided, inter alia, *that the assessees should build houses on the land within a specified time by using the best materials, that the lessors or their representatives would be entitled to supervise the building construction, and that after the expiration of 40 years the houses would belong to the lessors. Under the lease the assessees should pay the entire municipal tax in respect of the houses and a proportionate municipal tax in respect of the land. Upon acquisition of the land by the Government or by a public authority the lessors were entitled to all compensation in respect of the land but compensation in respect of the buildings was to be divided between the lessors and the assessees :*

Held, *that the assessees were the owners of the buildings until the period of the lease expired and they were therefore assessable under Section 9 of the Indian Income-tax Act in respect of the rents derived from the buildings.*

Commercial Properties Ltd., In re *[1928] (I.L.R. 55 Cal. 1057)* followed.

Cases referred to :—

Commercial Properties Ltd., *In re* [1928] (113 I.C. 848 ; I.L.R. 55 Cal. 1057 ; 32 C.W.N. 413 ; 3 I.T.C. 23).

Kaladan Suratee Bazaar Co., *In re* [1920] (56 I.C. 914 ; 1 I.T.C. 50).

Reference under Section 66 (1) of the Indian Income-tax Act (XI of 1922) by the Income-tax Appellate Tribunal : Income-tax Reference No. 4 of 1944.

STATEMENT OF CASE.

"This application under Section 66 (1) of the Indian Income-tax Act, 1922, has been filed by Ballygunge Bank Ltd., Calcutta. In this application, we have been asked to refer the following so called questions of law to the High Court, Calcutta. These questions are said to arise out of the order dated 26th June 1943 passed under Section 33 (4) in Appeal Case R. A. A. No. 91-Bengal of 1942-43.

The questions framed by the applicant are :—

(i) Where the assessee, a public limited company, with objects to acquire land by purchase, lease or otherwise, to deal in such land or to build houses thereon and deal in such houses or let out such houses, takes land on 40 years' lease and builds structures thereon on condition that the land together with the buildings thereon will revert to the lessor on the expiry of the lease and receives rents for such buildings from tenants, is the tax payable by the assessee in respect of rents so received to be determined in accordance with Section 9 or Section 10 ?

(ii) In view of the nature of the business carried on by the assessee company should it not be held that the letting out of the buildings in question and receipt of rent for the same came within the scope of the business the company had and as such assessable under Section 10 ?

(iii) Could it be held that having regard to the special condition of the lease by which both the land and the structures were to pass on to the lessor at the expiry of the lease the structures in question were the property of the assessee company as contemplated in Section 9 of the Act ?

2. The Commissioner of Income-tax, Bengal, the respondent to this application, in his reply mentions that the only question of law that arises is as under :—

" Whether in the circumstances of the case the rent derived from the buildings erected by the assessee company was properly assessed under Section 9 of the Indian Income-tax Act."

In our opinion a question of law arises and we proceed to state the case.

The applicant is a public limited company and its object, amongst others, is to acquire land by purchase, lease or otherwise, to deal in such land or to build houses and deal in such houses or let out such houses. For the assessment year 1941-42, it was assessed on an income of Rs. 25,523.

In this assessment a sum of Rs. 5,115 was included as an income from house properties under Section 9 of the Act. The assessee's case was that this income should be assessed under Section 10 and not under Section 9. The applicant's contention is that the applicant is not the owner of the house properties in question. The houses were built on lands taken on lease. The houses were then built and let out to the tenants. After the expiration of the period of lease the buildings would belong to the lessor. But this contention of the assessee was not accepted by the Income-tax Officer and on appeal under Section 30, the Appellate Assistant Commissioner confirmed the Income-tax Officer's action. This led to an appeal under Section 33 before this Tribunal. In an order dated 26th June 1943 passed under Section 33 (4) we dismissed the appeal holding that the assessment of the income from house properties was rightly made under Section 9 of the Act in this case for the reasons stated in the order. This gave rise to the application under Section 66 (1).

4. The only question of law that arises in this case is as follows and we refer it to the Honourable High Court, Calcutta, for its decision under Section 66 (1) of the Act:—

Question of law referred.—"Whether in the circumstances of the case the rent derived from the buildings erected by the assessee company was properly assessed under Section 9 of the Indian Income-tax Act."

5. In view of our reasons recorded in our order under Section 33 (4), it is not perhaps necessary to give in detail our reasons which lead us to come to the conclusion against the applicant. The applicant constructed the houses and got the income from these properties. It is immaterial that the houses would revert to the lessor after the expiry of the lease. For the present the applicant is unquestionably the owner. We are still of opinion that the case is covered by the decision of the Madras High Court in the case of *Commissioner of Income-tax, Madras* v. *Madras Cricket Club*[1]."

J. N. Majumdar with *R. B. Bakshi*, *Amal Kumar Mukherji*, *P. C. Basu*, *Sachindra K. Roy* and *Sushil K. Biswas*, for the assessee.

S. K. Gupta with *J. C. Pal*, for the Commissioner.

JUDGMENT.

GENTLE, J.—This reference under Section 66 (1) of the Income-tax Act is made by the Income-tax Appellate Tribunal at the instance of the assessee, the Ballygunge Bank, Ltd. The question referred for the opinion of the Court is:—

"Whether in the circumstances of the case the rent derived from the buildings erected by the assessee was properly assessed under Section 9 of the Income-tax Act?"

(1) (1934) 7 I.T.C. 290; 2 I.T.R. 209.

The assessees are a public limited company, one of their objects being to acquire land by purchase, lease or otherwise, to deal in such land or to build houses thereon and to deal in or let out such houses.

By deed of lease dated 28th February, 1936, the lessors let to the assessees, as lessees, a vacant piece of land (including a tank) of an area exceeding 6 bighas for the term of 40 years at a progressive monthly ground rent therein specified. The lease provided, *inter alia*, that:—

"Clause 5. The assessees would be entitled to parcel the land into a number of plots and to erect buildings, etc., thereon and to let out the same on hire and for the purpose of the same to lay out and construct lanes, streets, drains and sewers as might be necessary.

6. The assessees were entitled to construct, and would be held responsible for constructing, 25 separate and self-contained houses on the land at their own cost.

7. The assessees would use only the best available materials while constructing the buildings.

8. The assessees would construct at their own cost pucca structures; the position and detailed construction of each house and the number of rooms, storeys and dimensions thereof were left entirely to the assessees' discretion.

10. The existing tank and ditches to be filled in and levelled by the assessees.

11. Within 5 years after possession given of about 1 bigha 3 cottahs of land, the assessees would erect pucca structures and houses thereon after constructing pucca lanes, drains and sewers.

12. In case the assessees failed to comply with the conditions in clauses 10 and 11 the lessors would be entitled to take back possession of the entire land together with the buildings and houses erected thereon and the assessees would have no right to make objection thereto or to claim compensation in respect thereof.

14. After the expiration of the full period of 40 years the lessees 'will' take possession of the entire land together with all the structures and the assessees 'will' have no right, title or interest thereto and all the above 'will' pass to the lessors free from all encumbrances and defects.

18. The assessees to pay a proportionate part of the municipal tax in respect of the land and the entire municipal tax, from time to time levied, upon the structures to be erected.

22. In case of acquisition of the land by the Government or by any public authority (mentioned in the lease) any compensation received to be payable to the lessors whereas compensation in respect of the pucca structures would be apportioned according to the provisions contained in the lease on a graduated division dependent upon the unexpired period of

the lease when acquisition occurred; the lessor's share increasing as the period of the remaining term becomes less.

24. The lessors or their representatives to be entitled to visit the land or supervise any construction thereon on one day each week.

27. The assessees to be entitled to sub-lease the whole or any part of the land."

The assessees obtained possession of the land, filled in the tank, carried out the several works specified in the lease and erected houses on the land which they let to tenants, the assessees receiving the rents from the tenants.

In the assessees' income-tax assessment for the year 1941-42 there is included the sum of Rs. 5,115 for "property" which was assessed under Section 9 of the Income-tax Act. By Section 6 income shall be chargeable to tax under the head of "property"; by Section 9 tax is payable by an assessee under the head of "Income from property" in respect of the *bona fide* value of property consisting of any buildings or lands appurtenant thereto of which he is the owner.

It is not disputed that the amount of the assessment is correct. It is contended, however, by the assessees that they are not the owners of the houses but, under the lease, the lessors became the owners at the time they were constructed; further, the assessment should have been made under Section 10, as profits and gains of the business carried on by the assessees, it being their business to let out houses at rents.

The legal position, regarding the ownership of buildings constructed by a lessee upon land belonging to a lessor, is different in India to that in England. According to the maxim "*Quicquid planta tur solo, solo cedit,*" in England buildings and other things erected upon or affixed to the soil by a lessee, in the absence of a contract to the contrary, cannot be removed at the termination of a lease and become the property of the lessor. In India the position is governed by Section 108 (h) of the Transfer of Property Act which enacts that:—

"In the absence of a contract to the contrary.........

The lessee may even after the determination of the lease remove, at any time whilst he is in possession of the property leased but not afterwards, all things which he has attached to the earth: provided he leaves the property in the state in which he received it."

Therefore in India, when a lessee erects a house upon his lessor's land during the period of a demise, such house does not become appurtenant to the land but belongs to the lessee who can remove it, or demolish it and take away the materials, at the termination of the demise, unless there is a term to the contrary contained in the lease.

The lease granted to the assessee company contains a term which prevents removal of the houses erected during its currency. At the end of the tenure the houses undoubtedly will belong to the lessors but the present question is who is the owner during the currency of the lease.

Clause 18 of the lease requires the assessees to pay a proportionate amount of the municipal tax upon the land, but it further provides that the whole municipal tax upon the houses is to be paid by the assessees; which provision one would expect to find where the structures belong to a lessee. Upon acquisition of the land by the Government or by a public authority, clause 22 provides, in respect of the land, that the lessors shall have all compensation but, in respect of the buildings on the land, that is to be divided between the lessors and the assessees. If the buildings were the lessors' property they would be entitled to the whole compensation. This division reflects recognition of the assessees' expenditure and the ultimate right of the lessors to the property. The buildings erected by a lessee upon his lessor's land belong to the lessee who has the right, given by Section 108 (h) of the Transfer of Property Act, to remove them at the end of his tenancy. In the present case, clause 14 prevents the assessees from exercising that right and the structures will have to be left upon the land at the end of the term when, according to the clause, they will pass to the lessors. The lessors' right of ownership to the structures arises out of clause 14, which does not become operative until the expiration of the 40 years' term of the lease. At that time, and not earlier, the clause provides that the structures will pass to the lessors. The lease nowhere provides that the lessors become the owners of the structures upon their erection.

In my opinion, the lessors have no right of ownership in the structures until the lease determines by efflux ion of time; upon erection the assessees were the owners and their ownership continues throughout the period of the lease until its expiration when, and not before, the ownership will pass to the lessors.

The same position and effect would arise if clause 12 became operative which will not now occur, enabling the lessors to retake the land upon breach by the assessees of clauses 10 and 11.

Emphasis was sought to be placed upon clause 24, by which the lessors or their representatives are entitled to visit the demise and supervise the building construction, and clause 7, requiring the best materials to be used. I do not consider these clauses have the effect of making the lessors the owners of the houses. An owner of land, who leases it for the purpose of the lessee erecting houses upon it in accordance with the terms contained in the lease, is entitled to require the best materials to be used and to reserve to himself the right to see this is being done and to satisfy himself the structures are being properly built.

Since the assessees are the owners of the houses during the currency of the lease it is next to be considered how they should be assessed with respect to that property. The argument is that, since it is the assessee company's business to erect and let out houses at rentals, the assessment should be made under Section 10, upon the rents as profits and gains of their business and they should not be assessed under Section 9. Sub-section (1) of the latter section provides that:

"tax shall be payable by an assessee under the head 'income from property' in respect of the *bona fide* annual value of property consisting of any buildings or lands appurtenant thereto of which he is the owner, other than such portions of such property as he may occupy for the purposes of any business, profession or vocation carried on by him the profits of which are assessable to tax, subject to the following allowances, namely :—

(i) where the property is in the occupation of the owner, or where it is let to a tenant and the owner has undertaken to bear the cost of repairs, a sum equal to one-sixth of such value ;

(ii) where the property is in the occupation of a tenant who has undertaken to bear the cost of repairs, the difference between such value and the rent paid by the tenant up to but not exceeding one-sixth of such value ;

(iii) the amount of any annual premium paid to insure the property against risk of damage or destruction" ; and

(iv) the amount of interest paid upon a mortgage on the property and the amount paid in respect of an annual charge (not being a capital charge), ground rent, and interest upon borrowed capital used to acquire, construct, repair, renew or reconstruct the property ;

(v) land revenue ;

(vi) vacancies computed as therein specified."

The amount of the assessment is not the actual rent received from a tenant but it is the *bona fide* annual value (less the applicable deductions) which sub-section (2) of Section 9 defines as the sum for which the property might reasonably be expected to let from year to year. It is clear, from sub-section (1), that assessment pursuant to the section is applicable to property let to tenants. No distinction is made between ownership by an individual and ownership by a company. In *In re Commercial Properties, Ltd.*[1], a company's sole object was to acquire land, build houses and let them to tenants, it owned house property which it let to tenants, it was assessed under Section 9 and contended the assessment should have been made under Section 10. In the year of account, it was alleged, the company had sustained a loss upon its business of letting houses ; it was pointed out in the judgment, at page 1062, that in letting the houses, seeing to the payment of rent and (doubtless) doing the repairs, the company carried on business

(1) (1928) I.L.R. 55 Cal. 1057.

in the sense in which every landlord or owner of that type of property must necessarily carry on business. The argument was rejected that where the owner is a company, the objects of which include the object of owning and managing house property, the income derived from tenants is an income derived from business. With respect to the alleged loss incurred through unsuccessful trading with the property during the accounting year and the contention that the assessment should have been made under Section 10, in which event no income-tax would be recoverable, it was observed by Rankin, C.J., who delivered the judgment of the Court, at page 1062, that

"This is certainly a very important question, from the point of view of the treasury, because if this argument be right then it will depend to some extent upon the success of the management whether or not the public treasury should derive any income-tax in respect of house property of this character . . . . In my judgment, the words of Section 6 and Section 9 and Section 10 must be read so as to give some effect to the contrast that is there made between income, profits and gains from 'property' and from 'business'; and I entirely refuse my assent to the proposition that because it happens that the owner of a property is a company which has been incorporated for the purpose of owning such property, therefore, the income derived from 'property' must be regarded as income derived from 'business.' In my judgment, income derived from 'property' is a more specific category applicable to the present case."

In *In re Kaladan Suratee Bazaar Co.*[1], it was pointed out that a person or a company drawing income from house property was clearly not contemplated in the Indian Income-tax Act, as carrying on a business but was treated as a person who derived income from the property; also that a man who had invested his capital in house property and who kept a rent office and a staff of rent collectors for the purpose of letting his houses and collecting the rents, was not carrying on a business, he was merely taking the ordinary steps necessary for enjoying the income from his property. Reference was made to the above matters in the *Kaladan case*[1] at pages 1063 and 1064 of the judgment in the *Commercial Properties case*[2] which states that it is not favourable to the assessees. In the latter case it was held, at page 1066, that the facts and circumstances in that case came more directly and specifically under the word "Property" in Section 6 and the mere fact that the house owner was a company did not change the incidence of the tax and the Income-tax Act did not regard the income derived from ownership of buildings as profits of management.

The *Commercial Properties case*[2] is a decision by a Bench of three Judges of this Court and is binding upon us. It decided, as I understand it, that income derived from the ownership of buildings is chargeable to

(1) (1920) 56 I.C. 914. (2) (1928) I.L.R. 55 Cal. 1057.

tax under Section 9 irrespective of whether an individual or a company is the owner and also irrespective of whether one of a company's objects, or its sole object, is to acquire and let out buildings at rents ; ownership itself is the criterion of assessment under that section.

In my opinion the facts and circumstances of the present reference fall within the *Commercial Properties case*[1] and are completely covered by it. I would answer the question referred in the affirmative.

ORMOND, J.—I agree. *Reference answered in the affirmative.*

[IN THE ALLAHABAD HIGH COURT.]

HIRA MILLS LTD., CAWNPORE

v.

INCOME-TAX OFFICER, CAWNPORE.

SIR IQBAL AHMAD, C.J., and BRAUND, J. January 3, 1945.

INDIAN INCOME-TAX ACT (XI OF 1922), SECS. 3, 4 (1) (a), (c) ; 42 (1), (3) ; 66—NON-RESIDENT—INCOME, PROFITS OR GAINS—ACCRUED, AROSE OR WAS RECEIVED—BUSINESS CONNECTION—PROFITS DERIVED BY NON-RESIDENT COMPANY BY SELLING GOODS IN BRITISH INDIA THROUGH THEIR SALESMAN—ASSESSABILITY—APPLICABILITY OF SEC. 42 (3)—SCOPE OF SECS. 42 AND 4 (1)—SALE OF GOODS IN BRITISH INDIA THROUGH BROKERS WHO ARE NOT EMPLOYEES—WHETHER BUSINESS CONNECTION EXISTS—WHETHER PROFITS CAN BE DEEMED TO ACCRUE OR ARISE IN BRITISH INDIA.

The general charge of income-tax is imposed by Sections 3 and 4 of the Income-tax Act and the general charge is given a particular application in respect of a non-resident by Section 42 (1).

The charge of a non-resident to income-tax on profits and gains actually received or accruing or arising in British India is not, by virtue of the words "subject to the provisions of this Act," in any way modified by Section 42 (3).

The relief afforded by Section 42 (3) applies only to a case in which the profits and gains are deemed under Section 42 to accrue or arise in British India and not to a case in which they actually so accrue or arise or are received in British India.

The assessee, a non-resident company carrying on business of manufacturing cloth at Ujjain in the Gwalior State, sent cloth to Cawnpore in British India. The goods were sold by the assessee's salesman at Cawnpore and the sale proceeds were collected by him at Cawnpore :

Held, *that the profits and gains derived from the sales were assessable to income-tax on the ground that they were received in British India by or*

(1) (1928) I L.R. 55 Cal. 1057.

on behalf of the assessee within the meaning of Section 4 (1) (a) and also on the ground that they accrued or arose to the assessee in British India within the meaning of Section 4 (1) (c);

Held further, *that such profits and gains must be calculated without allowing any apportionment of that profit as between the period prior to the moment of export from Gwalior and the moment subsequent to that export.*

The cost to the assessee at the moment of sale in Cawnpore was the cost of, and other charges incidental to, the manufacture and export of them to Cawnpore and their sale there.

The assessee's goods were also marketed in British India through brokers who were not the assessee's employees and who were not canvassing orders exclusively for the assessee. Offers of purchase sent by brokers to Gwalior were not in any special form. They were either accepted or rejected by the assessee at Ujjain but contracts were all for delivery "F. O. R. Ujjain." Goods were generally consigned to "self" at the place of destination and the merchants took delivery by paying the invoiced price plus freight and insurance to a broker or bankers in British India and receiving in exchange an endorsed railway receipt:

Held, *that there was no "business connection" in British India and the income, profits or gains could not therefore be deemed to have accrued or arisen to the assessee in British India within the meaning of Section 42 (1).*

Case law discussed.

Quære—*Whether the profits or gains accruing or arising to the assessee can be reached by the British Indian Income-tax authorities under Section 4 (1).*

The High Court is not bound or entitled to propound a question of law which the Commissioner did not press before the Appellate Tribunal, either as an addition to, or as an alternative to, the one set up by the Appellate Tribunal.

It would be a practice more in conformity with Section 66 and with general convenience if the statement of case itself contained all the relevant facts rather than they should be sought for in the judgments.

Cases referred to:—

Commissioner of Income-tax, Bombay *v.* National Mutual Association of Australasia Ltd. [1933] (I.L.R. 57 Bom. 519; 35 Bom. L.R. 896; A.I.R. 1933 Bom. 427; 6 I.T.C. 426; 1 I.T.R. 350).

Commissioner of Income-tax, Bombay Presidency *v.* Bombay Trust Corporation [1930] (I.L.R. 54 Bom. 216; 57 I.A. 49; A.I.R. 1930 P.C. 54; 121 I.C. 532; 4 I.T.C. 312).

Commissioner of Income-tax, Bombay *v.* Remington Typewriter Company (Bombay) Ltd. [1931] (I.L.R. 55 Bom. 243; 33 Bom. L.R. 413; 130 I.C. 679; A.I.R. 1931 P.C. 42; 5 I.T.C. 177).

Commissioner of Income-tax, Burma *v.* Messrs. Steel Brothers & Co., Ltd. [1925] (I.L.R. 3 Rang. 614; A.I.R. 1926 Rang. 97; 94 I.C. 466; 2 I.T.C. 119).

Erischsen *v.* Last [1881] (8 Q.B.D. 414).

Nand Lal Bhandari Mills Ltd. (Cawnpore) *v.* Commissioner of Income-tax, Central and United Provinces [1939] (I.L.R. 1939 All. 832; 7 I.T.R. 452; 185 I.C. 99; A.I.R. 1939 All. 593; 1939 A.L.J. 631).

Pondicherry Railway Co. Ltd. *v.* Commissioner of Income-tax, Madras [1931] (I.L.R. 54 Mad. 691; 58 I.A. 239; 132 I.C. 619; 5 I.T.C. 363; A.I.R. 1931 P.C. 165).

Rogers Pratt Shellac & Co. *v.* Secretary of State for India [1925] (I.L.R. 52 Cal. 1; A.I.R. 1925 Cal. 34; 83 I.C. 273; 1 I.T.C. 363; 28 C.W.N. 1074).

Reference under Section 66 (1) of the Indian Income-tax Act (XI of 1922) by the Income-tax Appellate Tribunal (Bombay Bench): Miscellaneous No. 392 of 1943.

STATEMENT OF CASE.

" This is an application by the Hira Mills Ltd., Cawnpore, asking us to refer certain questions of law stated to arise out of our judgment in the applicant's Regular Assessment Appeal No. 49/U.P. of 1941-42, for the opinion of their Lordships of the Allahabad High Court, under Section 66 (1) of the Indian Income-tax (Amendment) Act, 1939. The Commissioner of Income-tax, C.P. and U.P., has filed a written answer stating that only one question of law arises for reference. The application and the written answer are exhibits A and B, respectively, and a copy of our judgment in the Regular Assessment Appeal is exhibit C.

2. Here it may be mentioned that the applicant's Regular Assessment Appeal No. 49/U.P. of 1941-42 was heard and disposed of by us (Bombay Bench) having been made over to us by an order of the President. Consequently, we are submitting this reference to their Lordships.

3. The questions that arise on this reference relate to an assessment made upon the applicant Mills for the charge year 1939-40. It was confirmed in appeal by the Appellate Assistant Commissioner, Agra. Copies of the Income-tax Officer's and the Appellate Assistant Commissioner's orders are, respectively, exhibits D and E.

4. The material facts, undisputed as well as those found established on evidence, have been narrated in paragraphs 2 and 3 of our judgment. We restate them very briefly for the purpose of this reference. The applicant is a 'non-resident' company registered in the Indian State of Gwalior where it manufactures cloth in its textile mills situated at Ujjain. In the year of account the total sales of the manufactured goods amounted to about 32 lakhs of rupees in round figures. But the assessee's appeal before us related only to sales amounting to Rs. 8,71,132 out of which, in return, those amounting to Rs. 3,83,305 were made at Cawnpore in British India, and the rest amounting to Rs. 4,87,827 from Ujjain. The assessee company sent its goods to Cawnpore where they were sold on its behalf by a salesman whom it had engaged on a monthly allowance by way of a wage or salary. As regards Ujjain sales they were made to customers in British India through brokers who also did business in British India. The manner in which these sales were made is described in detail in para. 3 (b) of our judgment.

5. The total profit that the assessee company made on both kinds of sales admittedly amounted to Rs. 73,471 in the year of account. The

Income-tax Officer brought the whole of this profit to taxation holding that it was income either received or accrued in British India, within the meaning of Section 4 (1) (c) or Section 4 (1) (a) of the Indian Income-tax Act.

6. The assessee company contended before the Income-tax authorities as well as before us that the income, profits or gains from Cawnpore sales did not actually accrue or arise in British India, although they might be deemed to have done so under Section 42 (1) of the Indian Income-tax (Amendment) Act, 1939. Consequently, it was urged that these profits could only be assessed on a proportionate basis, under Section 42 (3) of the Act, inasmuch as all the operations of the company's business were not carried out in British India. With regard to the profits from Ujjain sales the case was that they were not at all liable to taxation under the Income-tax Act inasmuch as they had wholly accrued or arisen out of British India. Alternatively, it was contended that if these profits were at all taxable that could only be on the footing of their being deemed to have accrued or arisen in British India under the provisions of Section 42 (1) and (3) of the Act.

7. We held that the whole of the profits from Cawnpore sales accrued to the non-resident assessee in British India and were therefore taxable under Section 4 (1) (c). We also held that the element of receipt of profits at Cawnpore also made them liable to be assessed under Section 4 (1) (a) of the Act. We accordingly upheld the view taken by the Income-tax authorities with regard to these profits. As regard Ujjain sales we differed from the Income-tax authorities and held that the profits from these sales must be deemed to have accrued to the assessee in British India within the meaning of Section 42 (1) and that, therefore, they could be only assessed on a proportionate basis under the provisions of Section 42 (3).

8. Before proceeding to comment upon the question for reference proposed by the assessee and formulate those that really arise for reference we must refer to a contention made in the present application that there was no evidence to support our finding of fact that the whole of the profits from Cawnpore had been received at that place. It is therefore contended that our finding that these profits were assessable under Section 4 (1) (a) on receipt basis was wrong on account of the basic error in a finding of fact with regard to the receipt of profits at Cawnpore. In the first place, we must observe that the fact of receipt of profits at Cawnpore where goods were actually sold to customers by the assessee's salesman was not in dispute before us, and the appeal proceeded upon a common ground that the whole of the profits were so received there. At any rate, we respectfully point out that our finding that the whole of the Cawnpore profits were assessable to tax was based on the view that they had accrued to the non-resident company in British India and fell within Section 4 (1) (c). That was our main finding. We disposed of the point of receipt by a brief sentence at the end of paragraph 6 of our judgment ;—

" The element of receipt in Cawnpore also makes them assessable under Section 4 (1) (a) of the Act."

The reasons for our findings regarding the liability of both kinds of profits are set out in paragraphs 4 to 8 of our judgment.

9. Broadly speaking the two points of law that would arise for reference are whether the profits in respect of Cawnpore sales accrued to the assessee company in British India, and whether those in respect of the Ujjain sales should be deemed to have accrued to the assessee company in British India. The assessee has however formulated not less than ten questions on these two points, out of which the first three relate to the Cawnpore profits and resolve into one. The fourth and the fifth questions are abstract questions of law and cannot be referred. The sixth question raises a point as to whether Sections 4, 4-A and 4-B of the Act are *ultra vires* of the legislative powers of the Central Government. This question was not raised in the appeal nor debated in the arguments, and therefore cannot be said to arise out of our judgment. Question No. 7 as to whether there was any evidence of the profits of Cawnpore sales being received in British India has been disposed of by us in the above paragraph. Questions 8 to 10 relate to Ujjain sales and really involve but one question.

We think therefore that only two questions arise for reference in this case which we formulate as below :—

Questions referred.—(1) Whether, on the facts of the case, the profits and gains derived from sales made at Cawnpore by the assessee's salesman of the goods manufactured by the assessee at Ujjain outside British India were rightly held to accrue or arise to the assessee in British India within the meaning of Section 4 (1) (c) or received in British India by or on behalf of the assessee within the meaning of Section 4 (1) (a) of the Indian Income-tax (Amendment) Act, 1939 ?

(2) Whether, on the facts of the case, the profits and gains derived from sales made from Ujjain to customers in British India through brokers in British India were rightly held to be the profits or gains deemed to have accrued or arisen to the assessee company in British India within the meaning of Section 42 (1) and assessable under sub-section (3) of that section ? "

Para. 3 (b) of the judgment of the Appellate Tribunal which describes in detail how Ujjain sales were made is as follows :—

" The facts relating to the Ujjain sales are however somewhat different, and are not without contest on one or two points. The company sells its goods to purchasers in British India, through brokers who also carry on their business in British India. These brokers are not regularly employed by the assessee company nor do they exclusively work for it. They canvass orders from buyers in British India and forward the offers to the assessee

company at Ujjain for acceptance. These offers are forwarded by means of ordinary letters or on contract forms used by the merchants or brokers in the usual course of their business. If the contracts are accepted, the assessee company, in the former case, reduces the offer to writing on contract forms of their own and sends them to the purchasers for their signatures through brokers. In the other case, it simply endorses its acceptance on the forms forwarded by the broker or the buyer. In either case, the acceptance is endorsed by the company at Ujjain. In paragraph 5 of his order the Appellate Assistant Commissioner has remarked that in some cases the contract forms are signed by the brokers as agents of the company. This fact however is not admitted. The assessment order of the Income-tax Officer makes no reference to it, and, on the contrary, a passage from a letter of the assessee's accountants quoted by him, as well as by the Appellate Assistant Commissioner, indicates that the brokers only canvass orders and transmit the offers to the company for acceptance at Ujjain. In this connection, three contract forms were produced for our inspection and are on record. They do not bear out the particular observation of the Appellate Assistant Commissioner. In one case, however, the printed form appears to be signed by the broker over a printed designation of 'salesman.' But it is not the case for either side that the company has engaged any salesman in British India in the case of Ujjain sales. The Appellate Assistant Commissioner has also remarked that in some cases the brokers have prevailed upon the company to agree to a reduction in prices. But that is not borne out by the record. Thus the facts established are that brokers in British India canvass orders from buyers and forward them for the company's acceptance at Ujjain where also the acceptance is endorsed. Then as regards the sales themselves admittedly the goods are forwarded by the company F.O.R. Ujjain. The relative railway receipts are forwarded to the purchasers either through the brokers or bankers."

JUDGMENT.

This is a reference under Section 66 (1) of the Indian Income-tax Act, 1922, by the Income-tax Appellate Tribunal (Bombay Branch). The assessee is a company called the Hira Mills Ltd., (hereinafter called the assessee), which is registered at Ujjain in Gwalior State. The business of the assessee is to manufacture cloth and its mills are situated at Ujjain. The assessee is accordingly a non-resident company for the purposes of the Indian Income-tax Act, 1922. Two questions said to be questions of law, have been set up by the Income-tax Appellate Tribunal in the statement of the case which it has submitted. The first is, we think, readily answered, but the second is one of difficulty.

The first question relates to the profits and gains of the assessee derived from the sale of cloth at, or through, its establishment at Cawnpore in British India. In the accounting year the assessee sold its cloth manufactured in Gwalior at Cawnpore to the value of Rs. 3,87,305 gross, and the Income-tax Department has for the year 1939-40, the assessment year in question, sought to tax the assessee under Section 4 (1) (c) upon the entire profits attributable to these gross sales, without allowing any apportionment of that profit between what is attributable to the manufacturing process in Gwalior up to the point of export from that State and what is attributable to the import into, and sale in, British India.

The facts, as stated in the case submitted to us, show that the assessee maintains a salesman of its own at Cawnpore, to whom it makes a monthly allowance by way of wage or salary. This we take to mean that the salesman at Cawnpore is nothing more or less than a paid employee of the assessee at Cawnpore. The goods imported from the assessee's mills in Gwalior are then sold by the assessee's salesman in Cawnpore and it is not in dispute that the whole of the sale proceeds are collected by the assessee's salesman at Cawnpore.

The contention of the assessee before the Income-tax Appellate Tribunal was that the Cawnpore sales, being the result of an initial process of manufacture and production in Gwalior, could not be said to have produced profits and gains which accrued or arose wholly in British India within the meaning of Section 4 (1) (c) of the Act, and must therefore, if assessable at all, be assessed as profits and gains which are merely deemed to accrue or arise under Section 42 (1) of the Act and are, as such, entitled to the benefit of the apportionment allowed by sub-section (3) of Section 42. The question actually set by the Tribunal is this :—

"(1) Whether, on the facts of the case, the profits and gains derived from sales made at Cawnpore by the assessee's salesman of the goods manufactured by the assessee at Ujjain outside British India were rightly held to accrue or arise to the assessee in British India within the meaning of Section 4 (1) (c) or received in British India by or on behalf of the assessee within the meaning of Section 4 (1) (a) of the Indian Income-tax (Amendment) Act, 1939 ?"

We think that this question is most easily disposed of on the ground, which has been noted by the Tribunal, that the profits and gains in question were actually received by or on behalf of the assessee in British India and are, therefore, assessable under Section 4 (1) (a) of the Act. That the gross profits indeed, the gross sale proceeds, were received in British India is not to be disputed. The answers given to this by the assessee are, first, that Section 4 of the Indian Income-tax Act does not apply at all to a non-resident, by virtue of the special provision made for him in Section 42,

and, secondly, that even if that is not so, Section 4 (1) is introduced by the words "subject to the provisions of this Act," which would suffice, even in the case of profits and gains received in British India, to entitle them to the benefit of Section 42 (3). In our view, neither of these arguments can succeed. As to the former, we cannot accept it that Section 42 (1) of the Act can be divorced from Sections 3 and 4, so as to subject a non-resident assessee to a charge of income-tax arising only under Section 42, and not under Sections 3 and 4. We appreciate, following the view expressed in *Rogers Pratt Shellac & Co.* v. *Secretary of State for India*[1], and *Commissioner of Income-tax, Bombay* v. *National Mutual Association of Australasia Ltd.*[2], that Section 42 of the Indian Income-tax Act is a charging section in the sense that, as the learned Chief Justice of Bombay has pointed out in the latter case at page 527, it does have the effect of rendering a non-resident liable to tax in respect of sources of income to which he would not be liable to tax if because a resident. In that sense it is, of course, a charging section but that is a long way from saying that Section 42 (1) has to be read independently of the general charging sections. It seems to us that the truth is that the general charge of income-tax is imposed by Sections 3 and 4 and that the general charge is given a particular application in respect of a non-resident by Section 42 (1). Neither can we accede to the alternative proposition that the charge of a non-resident to income-tax on profits and gains actually received or accruing or arising in British India is, by virtue of the words, "subject to the provisions of this Act," in any way modified by Section 42, sub-section (3). We think on construction alone that it is quite clear that the relief afforded by Section 42, sub-section (3), applies only to a case in which the profits and gains are deemed under Section 42 to accrue or arise in British India, and not to a case in which they actually so accrue or arise or are received in British India. Indeed, this is what the sub-section says. It in terms applies only to the profits and gains of a business "deemed under this section to accrue or arise in British India......." We are unable, therefore, to read the sub-section as amounting to a general proviso applied to profits and gains received, accruing or arising under Section 4, which is the section clearly applicable in this case to the Cawnpore profits of the assessee. Dismissing, therefore, sub-section (3) of Section 42 of the Act, we are bound to look at the language of Section 4 and to interpret the meaning of the words "profits and gains." There is no reason for giving to these words anything but their usual meaning of the difference between the gross cost to the seller of the goods at the moment and at the point of sale and the net price which he receives. The seller at Cawnpore was unquestionably the

(1) (1925) I.L.R. 52 Cal. 1.

(2) (1933) I.L.R. 57 Bom. 519, at p. 532; 1 I.T.R. 350.

assessee. The cost to the assessee at the moment of sale in Cawnpore was the cost of, and other charges incidental to, the manufacture and export of them to Cawnpore and their sale there. The circumstance that the assessee produced the goods in an Indian State can make no difference to the meaning of the words "profits and gains," and, if the true construction of the Act gives rise, in this, as in other cases, to double taxation, that is not a matter by which we can be influenced in construing the Indian Income-tax Act. If assistance were needed in reaching this conclusion, it is afforded by the case of *Erichsen* v. *Last*[1], in which a very similar contention in a different context was rejected by the English Court of Appeal. Our attention has been drawn to the decision of the High Court of Burma in *Commissioner of Income-tax, Burma* v. *Messrs. Steel Brothers & Co., Ltd.*[2] But, even in this case there is no decision that the profits and gains of one continuous process between manufacture and sale can be apportioned so as to give rise to two processes, one, up to the point of export of the manufactured article, and the other, from that point onward until final sale. It is true that it was held in that case that, where there was the reverse operation of manufacture in India and sale in England, the non-resident company in England which handled the selling organization of the goods produced by its own branch in Burma was entitled to deduct a proper commission from the profits accruing or arising in British India in consideration of its sales services. This, however, would appear to us, with great respect, to be a little difficult to understand as it is not easy logically to see how, if the net profits and gains received in England by Messrs. Steel Brothers & Co., Ltd., were taxable in British India as profits and gains accruing and arising in Burma, those net profits could again be diminished by deducting from them a sum for commission payable to the assessee company itself which would in effect represent a further taxable profit.

We must, therefore, answer this first question by saying that the profits and gains referred to therein were rightly held both to have been received in British India by or on behalf of the assessee within the meaning of Section 4 (1) (a) of the Indian Income-tax Act, 1922, as amended, and also to have accrued or arisen to the assessee in British India within the meaning of Section 4 (1) (c) of the same Act. We feel it right to add, as was obviously intended by the case and since it has formed the sole subject for argument before us, that such profits and gains derived from sales made at Cawnpore by the assessee's salesman of the goods manufactured by the assessee at Ujjain must be calculated without allowing any apportionment of that profit as between the period prior to the moment of export from Gwalior and the moment subsequent to that export.

(1) (1881) 8 Q.B.D. 414. (2) (1925) I.L.R. 3 Rang. 614.

The second question is more difficult. It is :—

"(2) Whether, on the facts of the case, the profits and gains derived from sales made from Ujjain to customers in British India through brokers in British India were rightly held to be the profits or gains deemed to have accrued or arisen to the assessee company in British India within the meaning of Section 42 (1) and assessable under sub-section (3) of that section?"

The facts relating to this question, so far as they have been stated to us, deserve careful attention. The assessee's goods are also marketed in British India in other ways besides the sales through the medium of their Cawnpore salesman. The following, as we understand it from the statement of the case, is the method employed.

Brokers in British India, who are not the employees of the assessee, are, as part of their own business, in the habit of canvassing orders from purchasers of cloth in British India. There is nothing in the case to lead us to suppose that these brokers are in any sense specially engaged by the assessee. It has not been found that they canvass orders exclusively for the assessee; neither is there anything to establish either that individual brokers are "retained" by the assessee, or that the assessee has any special arrangement with any particular broker or brokers to canvass systematically on its behalf. The brokers are "free-lance" brokers, and, so far, at least, as the assessee is concerned, are at liberty to place the orders obtained by them where they will. We are vouchsafed no information as to the supply of catalogues or other canvassing material by the assessee to the brokers. Offers of purchase obtained by the brokers are, in paragraph 3 (b) of the Appellate Tribunal's judgment, stated to be first sent by the brokers to the assessee at Ujjain for acceptance or rejection either by letter or on the brokers' own contract forms used in the general course of their business. We understand that the brokers did not use any special form in the case of the assessee's business. The assessee then either endorsed its acceptance or its refusal, and it is mentioned in the assessment order that in the great majority of cases this was done over a Gwalior State stamp. The broker's accepted form was then returned to the broker for the purchaser's signature. Apparently the contracts are all for delivery "F. O. R. Ujjain." Nothing is stated in the case as to who the actual consignee is; but we understand that the goods are generally consigned to "self" at the place of destination, while the railway receipts are sent (to take the words of the Appellate Tribunal's judgment) "by the applicant," *i.e.*, the assessee, "to the purchasers through the said brokers or bankers." The Appellate Tribunal in paragraph 7 of its judgment says that "presumably, also, the goods were paid for at Ujjain." The actual facts, however, appear to be that the purchasing merchant took delivery by paying the invoiced

price, plus freight and insurance, to a broker or bankers in British India and receiving in exchange an endorsed railway receipt. The original assessment order only mentions payment through brokers. If the question had been one under Section 4 (1) (a) or 4 (1) (c) of the Act, it might have been very material to know more exactly in what capacity such bankers and brokers received these payments.

Those, as we understand them, are the facts to be gathered from the statement of the case and the accompanying judgments and orders. Perhaps we may properly observe that it would be a practice more in conformity with Section 66 (1) of the Act and with general convenience, if the statement of the case itself had contained all the relevant facts, rather than that they should have had to be sought for in the judgments. No question of law is raised by the question submitted to us whether, in the circumstances set out above, the profits on such sales as we have described were actually "received" or "accrued" or "arose" in British India under Sections 4 (1) (a) and 4 (1) (c) of the Indian Income-tax Act. The question is expressly and distinctly confined to Section 42 (1) of the Act. The Appellate Tribunal, in fact, itself decided that the profits were not "received" and did not "accrue" or "arise" in British India, and in his reply dated the 15th May 1943 to the statement of the case the Commissioner took exception to the omission from the question of law stated by the Tribunal of any reference to Sections 4 (1) (a) and 4 (1) (c) of the Act and himself submitted an alternative question, which raised no issue under Section 42 (1), but rested solely on Sections 4 (1) (a) and 4 (1) (c). Which of these two alternatives was right we do not feel called upon to consider, since the only question of law which has come before us to be considered is the one under Section 42 (1) of the Act propounded by the Appellate Tribunal. The Commissioner, had he been so minded, could have required the Tribunal to submit the question propounded by him, either alternatively, or in addition, to its own, and, if the Tribunal had refused, the Commissioner could have taken steps under Section 66 to compel it to state that question. But the Commissioner has not taken that course, though obviously alive to it, and we do not think therefore, that we are bound, or, indeed, entitled, to propound for ourselves a question of law, which apparently the Commissioner decided not to press, as an alternative to the only one set up by the Appellate Tribunal.

We have, therefore, to consider in short whether the income, profits or gains which accrued or arose, directly or indirectly, to the assessee from the transactions we have endeavoured to describe accrued or arose "through or from any business connection in British India." We think that the answer must be in the negative. The relevant words of Section 42 (1) of the Act are these ;—

"All income, profits or gains accruing or arising, whether directly or indirectly, through or from any business connection in British India...shall be deemed to be income accruing or arising within British India......"

Our attention has been called to many of the authorities which have been decided by the Judicial Committee and by Indian Courts as to the application of the words "business connection" to various sets of circumstances in which a non-resident has had dealings of one sort or another in British India. But we think that, in solving a question which must necessarily depend on particular facts, it is impossible to obtain more than general guidance from other cases involving very different facts. The truth perhaps is that the expression "business connection" in Section 42 (1) of the Indian Income-tax Act is one which permits of no precise definition. No definition of it is given by the Act itself and the legislature has apparently deliberately chosen to use words of wide, if uncertain, meaning.

In the case of *Commissioner of Income-tax, Burma* v. *Messrs. Steel Brothers & Co., Ltd.*[1], the Rangoon High Court took the view that the expression "business connection" was limited by the use of the word "business" and by the explanation of that word contained in Section 2 (4) of the Act, to such a connection as amounts to a business establishment in the opposite territory, and regarded it as a "compendious expression to cover such concerns in the nature of trade, commerce, or manufacture as arise through a branch, factorship, agency, receivership or management." In other words, they thought that there must be something in the nature of a definite trade, commercial or manufacturing establishment to constitute a "business connection." With respect, we are inclined to share the view of the learned Judges of the Bombay High Court in *Commissioner of Income-tax, Bombay* v. *National Mutual Association of Australasia Ltd.*[2], that this places too narrow a construction on the words "business connection." In the plain English, the word "connection" may be used in two slightly different shades of meaning. It may be used to denote an abstract connection in the sense of a bond with, or an interest in, some opposite place or person; or it may be used in a concrete sense to mean the opposite person or unit, himself, or itself, in some other place. The expressions, "I have had connections with Bombay for many years" and "I have a connection by marriage in Bombay," employ the word "connection" in two slightly different senses. It may be that the use of the words "business connection in" (as opposed to with) in Section 42 (1) of the Indian Income-tax Act lays some slight emphasis on the more concrete meaning of the word "connection," but, nevertheless, we think it limits it too much to confine it to some definite organization, establishment or entity being in the nature itself of an operating business branch or agent of the potential assessee.

(1) (1925) I.L.R. 3 Rang. 614, at pp. 652, 653.
(2) (1933) I.L.R. 57 Bom. 519, at pp. 528, 535; 1 I.T.R. 350.

In the case of *Rogers Pratt Shellac Co.* v. *Secretary of State for India* [1], the facts were that an American company had a branch office in Calcutta and a factory in the United Provinces, which pointed to a "business connection" in a concrete sense. In *Commissioner of Income-tax, Bombay Presidency* v. *Bombay Trust Corporation* [2], it was held that a company incorporated in Hong Kong to carry on a finance business, which used virtually its entire capital by way of loan to a company with similar objects in Bombay, had a "business connection" in British India. In that case there was a definite operating unit in British India with which the Hong Kong company was connected. The case of *Commissioner of Income-tax, Bombay* v. *Remington Typewriter Company (Bombay) Ltd.* [3] is probably the strongest illustration of a concrete "business connection," since in that case the American parent company had established subsidiary companies in India to operate its patents, which subsidiaries it completely controlled. In the *Pondicherry Railway case* [4], the question of "business connection" did not arise since the case turned on where the profits or gains were received. These, we think, are all cases where the non-resident company sought to be assessed had a very definite "business connection" in British India in the sense of an organized entity, either controlled by itself or working for it under its direction. In the case in our own Court of *Nand Lal Bhandari Mills Ltd., Cawnpore* v. *Commissioner of Income-tax, Central and United Provinces* [5], there was again a definite branch of the non-resident manufacturing company in British India, although it had not been established by the manufacturing company itself, but by its managing agents, who were also non-resident. It was held—and, if we may with respect say so, rightly held—that there was a business connection in British India between both the non-resident manufacturing company and the non-resident firm of managing agents and the Cawnpore branch, which sold the products of the manufacturing company, managed by the non-resident firm. At first sight it would appear that the case of *Commissioner of Income-tax, Bombay Presidency and Aden* v. *National Mutual Association of Australasia* [6] was a case of a non-resident company having a "business connection" in British India in a more abstract sense. But when the facts of this case are examined from the earlier report in *Commissioner of Income-tax, Bombay* v. *National Mutual Association of Australasia* [7], it appears that here again the assessee had its head office at Melbourne and maintained a branch office in the Bombay Presidency. This case was, therefore, another in which the non-resident had a connection in British India with or through which it did business of

(1) (1925) I.L.R. 52 Cal. 1.
(2) (1930) I.L.R. 54 Bom. 216.
(3) (1931) I.L.R. 55 Bom. 243.
(4) (1931) I.L.R. 54 Mad. 691.
(5) (1939) I.L.R. 1939 All. 832; 7 I.T.R. 452.
(6) (1933) I.L.R. 57 Bom. 519; 1 I.T.R. 350.
(7) (1931) I.L.R. 55 Bom. 637.

its own creation and under its own control. We find, however, in this case an explanation of the meaning of the term "business connection" which, with great respect, we think approaches as nearly to a definition as is possible in the circumstances. Mr. Justice Rangnekar at page 534, after observing that the expression "business connection" is a comprehensive expression including not only those kinds of things specifically included by Section 2 (4) of the Indian Income-tax Act within the meaning of the word "business," but the kind of things which are specifically mentioned in the English Act, adds:—

"All that is necessary is that there should be a 'business' in British India and a connection between a non-resident person or company and that 'business,' and that the non-resident person or company has earned an income through such connection."

If we may respectfully adopt this language, we have, we think to ascertain whether the sales in British India effected by the assessee in the case before us in fulfilment of orders brought to it by British India brokers constituted a "business" of the assessee in British India and whether that "business" brought profits or gains to the assessee through any connection of the assessee with it. It becomes, therefore, a practical question.

The assessee, the Hira Mills Ltd., undoubtedly, by the means we have described, sold its cloth to the value of nearly five lakhs in British India during the accounting year. It had customers in British India. It traded with British India. We think, therefore, that there was a business in British India, in the limited sense that a substantial part of the assessee's output found its way into consumption in British India. The next question is whether there was a "connection" between the assessee and that business. In one way there was an obvious connection in that the assessee was the maker of the goods which were eventually consumed by British India buyers. But we do not think that it is a connection in such a loose sense as this that is contemplated by Section 42 (1) of the Indian Income-tax Act. On the facts, as proved, what other "connection" was there? The assessee had no branch, agency or establishment of its own in British India. We cannot discover any facts upon which it can be held even that the assessee, by an arrangement with British India brokers, had in effect constituted an agency for itself. The brokers were not, as far as we know, retained by the assessee. The assessee had no claim upon the goodwill of the brokers. The fact that the assessee may have paid the brokers a commission and certain out of pocket expenses, if and when they brought an offer which the assessee accepted, does not, we think, alter the circumstances. As we see it, on the proved facts, the position was that the assessee sold its goods in British India to a British India customer if and when that customer, either direct or through a broker, offered to purchase them by sending an order to Ujjain.

We do not think that this amounted to a "business connection in British India" from or through which the assessee derived the profits or gains on those transactions within the meaning of the authorities to which our attention has been drawn. They were sales to customers who happened to be in British India. It may be that, in the circumstances of this or any other particular case, the profits or gains accruing or arising to a non-resident from its sales in British India can be reached by the British India Income-tax authorities under Section 4 (1) of the Indian Income-tax Act. But that is quite a different thing from "deeming" them to have accrued or arisen in British India from or through a "business connection." In this case we do not think that there was any such "business connection" as falls within Section 42 (1) of the Act.

For these reasons, we think that the second question put to us should be answered in the negative.

As the applicant and the Income-tax Department have each succeeded and failed in one of the questions, we propose to make no order for the costs of this reference. A copy of this judgment will be sent to the Appellate Tribunal for the passing of such orders as are necessary to dispose of the case conformably with it.

We fix the fee of counsel appearing for the Income-tax Department at Rs. 500. There will be a period of one month from this date for him to file his certificate. *Reference answered accordingly.*

[IN THE ALLAHABAD HIGH COURT.]

BADAR SHOE STORES, *In re.*

BRAUND and MALIK, JJ. February 8, 1945.

INDIAN INCOME-TAX ACT (XI OF 1922 AFTER AMENDMENT IN 1939), SEC. 34—RE-ASSESSMENT—CIRCUMSTANTIAL EVIDENCE LEADING TO BELIEF OF UNDER-ASSESSMENT—WHETHER ASSESSMENT CAN BE RE-OPENED—"DISCOVERS," "DEFINITE INFORMATION," MEANINGS OF.

So far as the word "discovers" in the amended Section 34 of the Income-tax Act is concerned, it requires that the Income-tax Officer should have formed an honest and reasonable belief upon material which could reasonably support such belief. In the nature of things, it cannot amount to a conclusion of certainty. It is not necessary that, if the matter came to be subsequently decided in a Court of law, the Court should reasonably form the same conclusion as that formed by the Income-tax Officer.

What is a "discovery" and what is "definite information" must necessarily vary with the circumstances of the case. The words "definite information" are placed in Section 34 to protect the subject against an assault by an Income-tax Officer based upon mere suspicion. The "definite

information", which is something more than mere gossip or rumour, must lead to the discovery or "belief." Provided the information is definite and does lead to that belief, it need not necessarily be information of fact, though in ninety-nine cases out of a hundred it would inevitably be information of fact. Still less need it be information of actual escape from assessment or under-assessment. It may well be information of circumstances not themselves amounting to under-assessment or escape from assessment, but leading to the belief of under-assessment or escape from assessment. In short, it may be circumstantial evidence.

The assessee, a dealer in shoes, returned gross profits varying between 5 and 5·6 per cent. of the gross turnover for the four years including the accounting year 1939-40. As the return for the accounting year 1939-40 aroused the suspicion of the Income-tax Officer, he examined the accounts of that year in detail and found that an item on the debit side of the accounts had been inflated by a sum of Rs. 5,000. The assessee did not give any satisfactory explanation to this. The suspicions of the Income-tax Officer were also aroused in respect of the balances brought forward in 1939-40 accounts from previous years. Notice under Section 22 (4) for the production of accounts for the accounting years ending 31st March 1937, 1938 and 1939 was served on the assessee but the assessee stated that they were not available having been sold as waste paper. This was disbelieved by the Income-tax Officer. He came to the conclusion that probably the returned income in respect of the accounting year 1938-39 would, on investigation, prove false and therefore issued a notice under Section 34 of the Act stating that the assessee's income assessable to income-tax for the year ending 31st March 1940 had been under-assessed and requiring him to submit a return:

Held, *that the Income-tax Officer had, within the meaning of Section 34, "definite information" in consequence of which he discovered that the assessee's income of 1938-39 had escaped assessment in the assessment year 1939-40.*

The practice of omitting a sufficient statement of facts from the statement of case and of referring the High Court to other documents for the collection of the full facts necessary for determination of the question of law submitted, deprecated.

Cases referred to :—

Anderton and Halstead Limited v. Birrell ([1932] 1 K. B. 271; 101 L.J.K.B. 219; 146 L.T. 139; 47 T. L. R. 528; 16 Tax Cas. 200).

Commissioner of Income-tax, Bengal v. Mahaliram Ramjidas [1940] (8 I.T.R. 442; 67 I.A. 239; I.L.R [1940] 2 Cal. 215; 189 I.C. 154; A.I.R. 1940 P.C. 124; (1940) 2 M.L.J. 577).

Ingle v. Farrand ([1925] 2 K.B. 728; 11 Tax Cas. 446).

King v. Bloomsbury Income Tax Commissioners ([1915] 3 K.B. 768; 85 L.J.K.B. 129; 113 L.T. 1015; 31 T.L.R. 565; 7 Tax Cas. 59).

King v. Commissioners for the General Purposes of the Income Tax for Kensington ([1913] 3 K.B. 870; 83 L.J.K.B. 364; 109 L.T. 708; 6 Tax Cas. 279).

Williams v. Trustees of W. W. Grundy ([1934] 1 K.B. 524; 103 L.J.K.B. 204; 150 L.T. 378; 18 Tax Cas. 271; 2 I.T.R. 236).

Reference by the Income-tax Appellate Tribunal under Section 66 (1) of the Indian Income-tax Act (XI of 1922): Miscellaneous No. 162 of 1943.

JUDGMENT.

This is a reference by the Income-tax Appellate Tribunal under Section 66 of the Indian Income-tax Act at the instance of the Badar Shoe Stores (hereinafter called the assessee).

The statement of the case begins by saying that the necessary facts are set out in the judgment of the Appellate Tribunal and in greater detail in the assessment orders for the years 1939-40 and 1940-41. We deprecate the practice, which is becoming too common, of omitting a sufficient statement of facts from the statement of the case and of referring this Court to a miscellany of other documents for the collection of the full facts necessary for determination of the question of law submitted, and we shall take the opportunity of referring to the unfortunate consequences of this practice at a later stage of this judgment.

The assessee, a firm of which a certain Mr. Badr-Uzzaman was the proprietor, had carried on business as dealers in shoes at the Shoe Market, Agra, since at least the beginning of the year 1936. For the accounting year 1935-36 the gross profits returned by the assessee amounted to approximately five per cent. of the turnover of the year and in each of the subsequent four years, including the accounting year 1939-40, the gross profits returned varied between 5 per cent. and 5·6 per cent. of the year's gross turnover. In due course on the 18th July, 1940, the Income-tax Officer received the return of the assessee of the profits of the accounting year 1939-40 for the assessment year 1940-41. This disclosed that the gross income for the accounting year was Rs. 9,433, being a percentage of 5·6 of the turnover, and a net income of Rs. 2,050. These figures, apparently for the first time, aroused the suspicion of the Income-tax Officer and he, thereupon, examined the accounts of the accounting year 1939-40 in detail. As a result of this examination he found that on the 29th October, 1939, an item on the debit side of the accounts had been inflated by a sum of Rs. 5,000. The Income-tax Officer came to the conclusion that this was fraudulent and he caused a notice to be served on the assessee under Section 23 (2) of the Indian Income-tax Act to attend at his office. On the 6th August, 1940, the assessee's statement was recorded and, to put the matter shortly, the assessee had no explanation to give satisfactory to the Income-tax Officer, whose suspicions by this time had also been aroused in respect of the balances brought forward in the 1939-40 accounts from previous years. On or about the same date a notice was served on the assessee by the Income-tax Officer under Section 22 (4) of the Act calling upon him to produce, or to cause to be produced, his books of account for the accounting years ending 31st March 1937, 1938 and 1939, in addition to

those for the year 1939-40 already before the Income-tax Officer. This notice provoked the reply from the assessee on the 15th August, 1940, that his books for previous years were not available as, following the practice of his firm, "he apprehended" that they had been sold as waste paper by his Delhi office. The assessee attempted to produce some evidence to this effect, but it was disbelieved as a fact by the Income-tax Officer. The Income-tax Officer on the following day, on the 16th August, 1940, recorded the statement of the assessee to the foregoing effect. At the same time he issued a notice, which is Ex. T.-C. to the statement of the case, under Section 34 (1) of the Act stating that in consequence of definite information which had come into his possession he had discovered that the assessee's income assessable to income-tax for the year ending 31st March, 1940, had been under-assessed, and he required the assessee to deliver to him by a certain date a return in the form attached. It is to be noticed that this affected the assessment year 1939-40 in respect of the accounting year 1938-39, which was the year previous to the year in which the Income-tax Officer had found—we deliberately use a neutral word—the discrepancy of Rs. 5,000. Having, as the assessment order puts it, "got scent of the mischief" through the discrepancy of Rs. 5,000 in the year 1939-40 mentioned above, the Income-tax Officer then went through the books thoroughly for that year and discovered further discrepancies, amounting to inflation of purchases to the extent of a further three thousand and four hundred rupees, making Rs. 8,400 in all, and a reduction of cash balance to the extent of Rs. 10,000 in respect of the year 1939-40. The position, therefore, was, as we understand it, that, at the time the Income-tax Officer had actually served his notice under Section 34 in respect of the accounting year 1938-39, he had already, to his own satisfaction, actually found out a fraud to the extent of Rs. 5,000 in respect of the accounting year 1939-40, which subsequently led to his making further discoveries of the same kind in respect of the same year to the extent of a further Rs. 3,400 by way of inflation of purchases and Rs. 10,000 by way of reduction of cash balances. Moreover, at the time of the service of the notice on the 16th August, 1940, his suspicions had been thoroughly aroused as regards the balances brought forward in the books of the accounting year 1939-40 from the previous year.

We have had to collect these facts painfully rather from a number of documents included in the volume accompanying the statement of the case than from the statement of the case itself. The statement of the case, which is a relatively brief document, sums the matter up as we think, inaccurately in paragraph 6 by saying :

"It would appear from the above resume that the information that came into the possession of the Income-tax Officer, *viz.*,

(1) that the appellant had inflated purchases by Rs. 8,400;

(2) that he had attempted to reduce cash balances by Rs. 10,000; and

(3) that there were cash deposits in his books of account with regard to which he was unable to give any satisfactory explanation,

was actually obtained in the course of the assessment for the year 1940-41, and that all the irregularities that were noticed related in fact to transactions that took place during the financial year 1939-40 and not during the financial year 1938-39 whose income, profits and gains formed the subject-matter of the assessment in question........."

This may be true as far as it goes, but, in view of the real point raised by the question, it is very material to know exactly what the state of mind of the Income-tax Officer was at the time he served the notice of the 16th August, 1940, under Section 34 of the Income-tax Act in respect of the accounting year 1938-39. At that date he had already formed the definite conclusion in respect of the accounting year 1939-40 that there had been a fraud to the extent of at least Rs. 5,000. He suspected further frauds in respect of that year, which were not verified until later. Moreover, from the conclusions he had drawn from his discovery of the five thousand rupees fraud, he suspected the balances brought forward from previous years. He had actually formed a conclusion of fact that the assessee had told him a falsehood in respect of the disposal of his previous books as waste paper. In addition to these things, he had, on the 16th August, 1940, the following further facts before him. He knew that the assessee's returns of gross profits in each of the five years, including the accounting year 1939-40, had been shown at a uniform rate of 5 per cent. of the turnover. He had already found out that in respect of one of those years (the accounting year 1939-40) the rate of actual profit relative to the turnover had been substantially higher than 5 per cent. As appears from the assessment order itself, he knew that the assessee's business had been more or less uniform throughout those five years and he, therefore, based on these materials a conclusion of fact on the 16th August, 1940, that there was the likelihood of similar results in the previous accounting years. That is our analysis of the facts, which, as we have said, we have had to collect for ourselves rather than discover from the statement of the case. They can be summarized thus :—

(1) At the date of the relevant notice under Section 34, the Income-tax Officer had established to his own satisfaction an actual fraud in the books for the accounting year 1939-40;

(2) the Income-tax Officer had established to his own satisfaction that he had been told by the assessee a falsehood as regards the destruction of the books for the previous years, and

(3) the Income-tax Officer had reached the conclusion that, in the circumstances of his knowledge of the course of business over the whole

period of five years, there was a probability that, the returned income having proved false in one year, it would on investigation prove false in other years of that period also.

We can now approach the actual question of law put to us. We must concede that it is a question of law, because it involves not only the careful construction of the words of Section 34 of the Act, but the determination of certain principles of law involving such considerations as the degree of certainty in the mind of the Income-tax Officer required to constitute "definite information" and "discovery" within the meaning of the section. The actual question is in these words:—

"Whether, in the circumstances of the case, the Income-tax Officer had, within the meaning of Section 34, 'definite information' in consequence of which he could have discovered that the assessee's income of 1938-39 had escaped assessment in the assessment year 1939-40."

The use of the expression "in the circumstances of the case" is to be deprecated where those circumstances are not in fact set out in the case itself, but otherwise the question appears to cover the point involved. It is now necessary to turn to the section itself. It runs:—

"(1) If in consequence of definite information which has come into his possession the Income-tax Officer discovers that income, profits or gains chargeable to income-tax have escaped assessment in any year, or have been under-assessed, or have been assessed at too low a rate, or have been the subject of excessive relief under this Act the Income-tax Officer may......serve on the person liable to pay tax on such income, profits or gains......a notice......under sub-section (2) of Section 22, and may proceed to assess or re-assess such income, profits or gains........."

The construction of this section needs to be carefully approached. In the first place, it has to be observed that the section as amended in 1939 is radically different from the section prior to that amendment. Prior to the amendment, it provided that if, for any reason, income, profits or gains chargeable to income-tax had escaped assessment in any year or had been assessed at too low a rate, the Income-tax Officer might, at any time within one year after the end of that year, serve on the assessee a notice preliminary to re-assessment. This left it uncertain both whether the Income-tax Officer himself was to be the sole judge of whether circumstances had arisen to justify his action and as to the degree of certainty which was required from him. The amendment of 1939 is designed, we think, to dispel that uncertainty, and, therefore, it must be assumed that the legislature in laying down in the amended section the positive conditions in which the Income-tax Officer can take action intends those conditions to be strictly fulfilled. Section 34 as amended is, we think, not merely a section designed to afford the Income-tax Department a ready means of reopening

past accounts, but is also a section which is designed to protect the subject against anything in the nature of an inquisition at the instance of the department, founded on mere suspicion rather than on positive material. We think that, for the proper application of the amended Section 34 of the Indian Income-tax Act to any given set of circumstances, it is important to bear these considerations in mind. There are two things required by Section 34 to exist before it can be put into operation. First, there has to be in the possession of the Income-tax Officer and it must be in his possession at the date on which he puts Section 34 into operation "definite information." Secondly, the consequence of that "definite information" has to have been that, at the date at which he puts Section 34 into operation, he has "discovered" that income, profits or gains chargeable to income-tax have escaped assessment in any year, or have been under-assessed, or have been assessed at too low a rate, or have been the subject of excessive relief.

We shall take the second, or "discovers," part of the section first. On this there is considerable guidance to be obtained from English decisions under the Taxes Management Act, 1880, and the English Income Tax Act. We appreciate that great care has to be taken in using authorities relevant to the English Acts in construing an Indian Statute, and, although the material word "discovers" appears in the English Acts, it is not accompanied by the requirement that the discovery shall be the result of definite information. Nevertheless, we consider it legitimate to inform ourselves of the meaning that has been attributed to the word "discover" standing alone by English Courts in the context of the English Income Tax Act. Section 52 of the Taxes Management Act, 1880, provides that: "If the Surveyor discovers that any properties or profits chargeable to the duties have been omitted.........", then he may make an additional assessment.

The words of Section 125, sub-section (1), of the English Income Tax Act, 1918, are, so far as material, the same. In the case of *King* v. *Commissioners for the General Purposes of the Income Tax for Kensington* [1], three individual learned Judges of the English Court of Appeal have placed their several constructions on the word "discovers." Mr. Justice Bray says that it means "comes to the conclusion from the examination he makes and from any information he may choose to receive. There is nothing to prevent him from getting such information as he can..........."

Mr. Justice Avory said that in his opinion "the word means 'has reason to believe'."

Mr. Justice Lush says that:—"If we take 'discovers', as I think it was intended to be taken, as equivalent to 'finds' or 'satisfies himself' the difficulty disappears..........."

(1) [1913] 3 K.B. 870 ; 6 Tax Cas. 279.

The facts of that case were that the Surveyor had ascertained that at the material time a foreign company had existed and that the assessee had been carrying on a business in Bolivia. He had discovered material from which he was able reasonably to conclude that that business had been profitable and upon that the Surveyor had deduced that the assessee had omitted a return of his foreign possessions or of part of them. Admittedly, the Surveyor in this case had discovered substantial facts, but the importance of it is that the learned Judges, in the context of the English Act, placed upon the word "discovers" no higher meaning than that of having a reason—no doubt a legitimate reason—to believe. In any close analysis of a discovery in a non-physical sense, absolute certainty is never attainable and there must always be some element, however infinitesimal, of doubt in any human deduction. We think, with respect, therefore, that the word "discover" must necessarily always involve a measure merely of belief, and, provided that that belief is the belief of an honest and reasonable person based upon reasonable grounds, we have difficulty in seeing what further fulfilment of the word "discover" there can be. In *King* v. *Bloomsbury Income Tax Commissioners* [1], the Lord Chief Justice referred to the case of *King* v. *Commissioners for the General Purposes of the Income Tax for Kensington* (*ubi supra*) with approval and said himself that :—

"The Surveyor may be mistaken in the 'discovery', but if there is information before him upon which he could, and did honestly believe the person to be liable to the duties, the only remedy is by the appeal prescribed by the Statutes."

In *Ingle* v. *Farrand* [2], a case under Section 125 of the English Income Tax Act, 1918, the Master of the Rolls said that :—

"The Surveyor is not required to form an opinion, which is later held by the Courts to be the correct view, before he takes action. There must be information before him which would enable him, acting honestly, to come to the conclusion that a state of facts exists requiring him to take action........."

In *Williams* v. *Trustees of W. W. Grundy* [3], the word "discover" was extended to include a case in which an Income-tax Officer found out that certain income was chargeable to tax, which income his predecessor had thought not to be chargeable to tax. In that case the successor of the original inspector found out that a certain interest was merely a contingent interest and that upon that basis the income in question would be taxable. This was a "discovery" not of a physical fact but of the true construction of a certain document. Nevertheless, it was held to be a "discovery". On the other hand, there are cases to show that a mere change of opinion based on some

(1) [1915] 3 K.B. 768 ; 7 Tax Cas. 59.
(2) [1925] 2 K.B. 728 ; 11 Tax Cas. 446.
(3) [1934] 1 K.B. 524 ; 2 I.T.R. 236.

facts and figures does not amount to a "discovery": *Anderton and Halstead, Limited* v. *Birrell*[1]. The case of *Commissioner of Income-tax, Bengal* v. *Messrs. Mahaliram Ramjidas*[2] was decided by the Judicial Committee of the Privy Council on the unamended Section 34 and is, therefore, scarcely relevant to the amended section. Their Lordships of the Privy Council, however, took the view in respect of the unamended section that it was enough that the Income-tax Officer on the information which he had before him and in good faith considered that he had got ground for believing that the assessee's profits had for some reason escaped assessment or had been assessed at too low a rate.

Our conclusion from a consideration of these authorities is that, so far as the word "discovers" in the amended Section 34 is concerned, it requires that the Income-tax Officer should have formed an honest and reasonable belief upon material which could reasonably support such belief. In the nature of things, it cannot amount to a conclusion of certainty. It is not necessary that, if the matter came to be subsequently decided in a Court of law, the Court should necessarily form the same conclusion as that formed by the Income-tax Officer. The Income-tax Officer's belief, in the sense described above, is, to our minds, a "discovery" within the meaning of the Act.

We now come to the words "definite information." These present less difficulty, but it has to be remembered that both what is a "discovery" and what is "definite information" must necessarily vary with the circumstances of the case. We think that the words "definite information" are placed in Section 34 of the Indian Income-tax Act to protect the subject against an assault by the Income-tax Officer based upon mere suspicion. The "definite information", which is something more than mere gossip or rumour, must lead to the discovery, or "belief" as we have described it above. But we are not prepared to engage ourselves to the view that, provided the information is definite and does lead to that belief, it need necessarily be information of fact, though in ninety-nine cases out of a hundred it would inevitably be information of fact. Still less need it be information of actual escape from assessment or under-assessment. It may well be information of circumstances not themselves amounting to under-assessment or escape from assessment, but leading to the belief of under-assessment or escape from assessment. In short, it may be circumstantial evidence.

In the circumstances of the case before us, and applying the conclusions we have arrived at as to the true meaning of the words "discovers" and "definite information", we have come to the conclusion that, in respect of the notice under Section 34 of the Indian Income-tax Act served on the assessee by the Income-tax Officer on the 16th August, 1940, in

(1) [1932] 1 K.B. 271; 16 Tax Cas. 200. (2) [1940] 8 I.T.R. 442.

relation to the accounting year 1938-39, there was, at the time he served that notice, before him "definite information", in consequence of which he "discovered" that income, profits or gains of the year 1938-39 had escaped assessment or had been under-assessed. He had concluded a definite fact, *viz.*, that in the accounting year 1939-40 the assessee had falsified his books. It is true that that by itself was not direct evidence that he had falsified books in a preceding year. But the Income-tax Officer knew more than that. He knew that the low rate of profits to turnover for the preceding years, as returned by the assessee, had been the same as the rate of profit to turnover in the year in which the assessee had falsified his books. It appears to us that those two pieces of information, which had prior to the 16th August, 1940, come into the possession of the Income-tax Officer, constituted material of a definite nature from which he could form a reasonable belief—not certainty—that the assessee's profits in the previous years had escaped assessment. Nor does it end even there. He had "discovered" by the 16th August, 1940, not only that the assessee was a dishonest man in relation to his returns, but that he had deliberately withheld his books of account for the year 1938-39 and for years preceding that year. We must, we think, accept the Income-tax Officer's conclusion of fact upon this point—at any rate so far as his own state of mind was concerned—since we have no reason to doubt that it was a genuine and reasonable conclusion of fact. It is certainly not in appeal before us and there is nothing upon the record to show that it was a conclusion which the Income-tax Officer could not properly draw, leading to a belief that the assessee had made away with his books.

For these reasons we shall answer the question put to us in the affirmative.

The Commissioner of Income-tax will be entitled to the costs of this reference and we assess the fee of counsel representing the Commissioner at the sum of Rs. 200. A copy of this judgment will be sent under the seal of the Court and the signature of the Registrar to the Appellate Tribunal for such orders to be passed by them as are necessary to dispose of the case conformably with it.

Reference answered in the affirmative.

[IN THE ALLAHABAD HIGH COURT.]

COMMISSIONER OF INCOME-TAX, C. P. AND U. P.

v.

SHRI DWARKA DHEESH TEMPLE, CAWNPORE.

BRAUND and MALIK, JJ. January 4, 1945.

INDIAN INCOME-TAX ACT (XI OF 1922), SECS. 4 (3) (i), 66—CHARITABLE PURPOSES—TRUST FOR CONSTRUCTION OF TEMPLE—BALANCE OF FUND TO

BE INVESTED AND TO BE USED FOR PURPOSES OF TEMPLE—WORSHIP OPEN TO PUBLIC—INCOME USED FOR PUBLIC BENEFIT—WHETHER TEMPLE PUBLIC RELIGIOUS TRUST—QUESTION OF FACT OR LAW—WHETHER INCOME EXEMPT—WHETHER HIGH COURT ENTITLED TO GO BEHIND STATEMENT OF FACTS.

The assessee, a temple, was founded in 1883 and consecrated in 1886. An instrument of dedication executed in 1887 provided that a fund had been collected for the purpose of building and endowing the temple and a sum of Rs. 17,000 remaining after construction of the temple should be invested and used exclusively for the purposes of the temple and the donors had released all interest in it. The fund in course of time amounted to several lakhs of rupees. The income of the fund received by certain members of the original settlor's family as trustees was claimed by the Income-tax authorities as taxable. The Appellate Tribunal found that the public had from the very beginning exercised the right of going to the temple and worshipping the deity there, that the income was spent on Sadavart, Pathashala, Dharmshala etc., that these benefits were open to the public and that the properties of the temple had always been administered as belonging to a public trust:

Held, *that although it was not stated in the document whether the trust was a private or a public one and there was no presumption one way or the other, there was ample evidence for arriving at the conclusion that the assessee temple was a public religious trust and as such the income derived from the trust was exempt from taxation under Section 4 (3) (i) of the Indian Income-tax Act;*

Held further, *that no jurisdiction is entrusted to the High Court by Section 66 either to go behind or to question statements of facts made by the Appellate Tribunal in the statement of case.*

The issue whether property is held under trust for religious or charitable purposes raises both questions of fact and questions of law, or possibly mixed questions of fact and law.

Reference under Section 66 (1) of the Indian Income-tax Act (XI of 1922) by the Income-tax Appellate Tribunal: Miscellaneous No. 409 of 1943.

STATEMENT OF CASE.

"There are three applications by the Commissioner of Income-tax, Central and United Provinces, under Section 66 (1) of the Income-tax Act, asking the Tribunal to refer to the High Court certain questions which arise from the orders of the Tribunal passed respectively in R. A. A. No. 44 (U.P.) of 1941-42, R. A. A. No. 63 (U.P.) of 1942-43 and R. A. A. No. 64 (U.P.) of 1942-43. The three appeals relate to the assessment years 1939-40, 1940-41 and 1941-42 respectively. As the parties to these applications are

the same and the issues involved are identical, they have been consolidated and dealt with together.

2. In Chotai Mahal, Cawnpore City, there is a temple dedicated to Shri Dwarka Dheeshji, which was built by certain votaries of the deity in 1883 and consecrated in 1886. On July 11, 1887, an informal instrument of dedication was made the genuineness or validity of which is not in dispute. That document recites that a fund of Rs. 43,000 was created, and dedicated absolutely and irrevocably to Shri Dwarka Dheeshji, whose temple had already been built, and that neither the donors nor any members of the family had any further right to the same. The deed gave directions as to the manner in which the amount was to be expended or invested, as the case may be. In 1898, in connection with a civil dispute between two of the founders of the endowment regarding certain property endowed by one of them for the temple a finding was recorded by the Additional Subordinate Judge at Cawnpore, in Suit No. 11 of 1898, that the endowment in favour of Shri Dwarka Dheeshji was valid and irrevocable, having been duly and lawfully made and completed by delivery of possession. The testimony of L. Juggilal in that suit proves that the public were from the commencement exercising the right of going to the temple and worshipping the Thakusji. In a statement made by L. Ganga Prasad before us on April 21, 1942, which we accepted as true, it was definitely acknowledged that the income of the temple properties is spent on Sadavart, Pathashala, Dharmshala, Bhog, Utsav etc., that the public is permitted for all these, that they come in their own right, that every day about 100 to 150 persons of the public come to the temple for worship and their offerings are accepted, that never is anybody prevented from coming and worshipping in the temple and that there is no prohibition of any kind unless the person is drunk. The temple has throughout been treated as a place of public worship and its properties were always administered as belonging to a public trust. The small nucleus originally provided by the founders has in the course of half a century, by uniformly efficient management, been augmented to several lakhs, a considerable portion of which is invested in substantial immovable property.

3. In connection with the assessment for 1939-40, the Income-tax Officer assessed to tax the income of the endowment in the view that it was not a public religious trust but was merely a private religious trust, whose income did not enure for the benefit of the public. The Appellate Assistant Commissioner concurred in this view; but the Tribunal took a contrary view in its order in R. A. A. No. 44 (U. P.) of 1941-42. Upon a construction of the instrument of July 11, 1887, the Tribunal held that it afforded the clearest evidence of an absolute and irrevocable dedication, coupled with a complete divestiture by the owner of all beneficial interest in the fund

comprising the endowment. It was further held, taking into account the subsequent conduct of the concerned parties and the public, that the public had for over half a century used the shrine as a place for devotion and worship and that the fund has been wholly utilised, and the properties belonging to the endowment are entirely held and administered, as a public religious trust. The various grounds which were raised by the Income-tax authorities and the departmental representative were examined in detail, as also the judicial decisions bearing upon the point at issue, and in the end the Tribunal recorded the conclusion that the income from property belonging to the temple falls within the purview of clause (i) of sub-section (3) of Section 4 and accordingly directed that the assessment should be cancelled.

4. By the time these orders were passed the assessments for 1940-41 and 1941-42 had been completed by the Income-tax Officer on the lines adopted by him for the assessment of 1939-40, but the appeals preferred against the same by the assessee were pending with the Appellate Assistant Commissioner. In view of the afore-mentioned decision of the Tribunal granting the assessee immunity under Section 4 (3) (i) the Appellate Assistant Commissioner reversed the orders of the Income-tax Officer and cancelled the assessments in respect of those two years. The Income-tax Officer appealed to the Tribunal against the orders of the Appellate Assistant Commissioner and at the request of the departmental representative the whole question was examined once again in the light of the contentions advanced by him on behalf of the department. In the common order passed in the said appeal the Tribunal reiterated the conclusion that judging from the recitals in the instrument evidencing an unequivocal dedication and irrevocable divestiture, the uniform conduct of the donors and their families, the manner in which the fund was expended and administered as belonging exclusively to the deity, the fiduciary character avowedly borne by those who managed the funds and the properties belonging to the endowment, the rights exercised by the public in connection with the worship and offerings from the time of the consecration of the temple up to date, it was beyond doubt clear that the property was held as a public trust devoted wholly for religious purposes.

5. The Commissioner has now applied for a case being stated to the Court, suggesting that the following questions of law arise out of the orders of the Tribunal in all the three cases :—

'(1) Whether in the circumstances of the case the Shri Dwarka Dheesh Temple Trust, Cawnpore, is 'a private religious trust' as contemplated by Section 4 (3) (i) of the Income-tax Act ?;

(2) If so, whether the income derived by the trust enures for the benefit of the public and is as such exempt from the provisions of the said Act ?'

Item 10 of paragraph 5 of the application has been subsequently amended to correct an erroneous statement that was originally made as to the exact relief prayed for by the assessee in the appeal to the Tribunal.

6. The assessee's reply does not disclose any valid objection.

7. We are of the opinion that a common question of law arises out of the orders of the Tribunal in the three appeals above referred to and we accordingly refer to the High Court of Judicature at Allahabad under Section 66 (1) the following question:—

'Whether in the circumstances of the case the Shri Dwarka Dheesh Temple Trust, Cawnpore, is a public religious trust and as such whether the income derived by the trust is exempt from taxation under Section 4 (3) (i) of the Income-tax Act?' "

JUDGMENT.

This is a case stated to us under Section 66 of the Indian Income-tax Act by the Income-tax Appellate Tribunal. The assessee is a temple known as the Shri Dwarka Dheesh Temple of Cawnpore and the assessments which are brought into question are those for the assessment years 1939-40, 1940-41 and 1941-42.

The facts as stated by the statement of the case are relatively simple. It appears that the temple was founded in the year 1883 but was not consecrated until the year 1886. On the 11th July, 1887, there was what is described as an instrument of dedication. This document, which is Ex. T-K., dealt with a sum of Rs. 42,000 which had apparently been collected for the purpose of building and endowing the temple, and out of it Rs. 20,000 had been spent on the construction of the temple itself, a further Rs. 5,000 had been spent on ornaments and Rs. 17,000 remained to be disposed of. The deed declared that this balance should be invested in the purchase of a particular type of immovable property or should remain "deposited" at interest, and proceeded at some pains to make it quite clear that the donors of the fund had released all interest in it. It then in a somewhat inadequate way went on to provide for the management of the temple, but it is clear that some further and more comprehensive document was contemplated. However, as far as it goes, the instrument of the 11th July, 1887, makes it abundantly clear that the seventeen thousand rupees in question was to be used exclusively for the purposes of the temple.

In the interval of time between 1887 and now, the fund, of which the original Rs. 17,000 is now part, has multiplied itself many times over and we are told that it is now represented by a sum of several lakhs of rupees whether in money, property or investments and it is with the income of this substantial fund that we are now concerned. To put the matter shortly, the income is received by certain members of the original settlor's

family as trustees and the Income-tax authorities now claim that this income is taxable.

The question in the form in which it comes to us involves Section 4, sub-section (3), of the Indian Income-tax Act. That sub-section exempts from the charge of income-tax :—

"(i) Any income derived from property held under trust or other legal obligation wholly for religious or charitable purposes, and in the case of property so held in part only for such purposes, the income applied, or finally set apart for application, thereto."

This exemption is, however, qualified by a final proviso which runs thus :—

"In this sub-section 'charitable purposes' includes relief of the poor, education, medical relief, and the advancement of any other object of general public utility, but nothing contained in clause (i)......shall operate to exempt from the provisions of this Act that part of the income of a private religious trust which does not enure for the benefit of the public."

The answer, accordingly, given by the assessee to the Income-tax Officer is that the income in question is "derived from property held under trust for religious or charitable purposes." The Income-tax Officer, however, counters this by saying that the income in this case is merely the income of "a private-religious trust which does not enure for the benefit of the public." We concede that this issue raises both questions of fact and questions of law, or possibly mixed questions of fact and law.

Turning now to the statement of case, we have to see what facts are presented in order to decide the question of law set up. The question has been stated by the Income-tax Tribunal in the following language :—

"Whether in the circumstances of the case the Shri Dwarka Dheesh Temple Trust, Cawnpore, is a public religious trust and as such whether the income derived by the trust is exempt from taxation under Section 4 (3) (i) of the Income-tax Act?"

The facts stated by the Appellate Tribunal in their statement of the case are these. First, we are told that the public have from the very beginning exercised the right of going to the temple and worshipping the deity there. Secondly, we are told that the income of the temple properties is spent on Sadavart, Pathashala, Dharmshala, Bhog, Utsav etc., thirdly, that the foregoing benefits are open to the public, who come there to get them, in their own right. Fourthly, that every day some 100 or 150 members of the public come to the temple for worship and, fifthly, that there is no prohibition of any kind upon anyone having access to the temple, except the single qualification that he must be sober. Moreover, the Tribunal has stated as a fact that the temple has throughout been treated as a place of

public worship and its properties have always been administered as belonging to a public trust.

Now, those are the facts before us. The Income-tax department, which in this case is the applicant, makes a point of the circumstances that the instrument of 1887 is silent as to whether this trust is a public or a private trust. It is true that it is not stated in so many words in the document itself whether the trust is a private or a public one and there is no presumption one way or the other. When we look, however, at the course of events during the intervening fifty years stated as facts in the case now before us, no doubt can possibly be left in anybody's mind but that there was ample evidence upon what the Income-tax Officer could have concluded, as the Tribunal has now concluded, that this was a public, and not a private trust. We have been pressed hard by Mr. Pathak to go behind the statement of facts set out in the statement of the case by the Appellate Tribunal. The suggestion is that if we were to do this, we might find other facts which might or might not shake the conclusions of fact stated to us. As a matter of principle we do not think that any jurisdiction is entrusted to us by Section 66 of the Income-tax Act either to go behind or to question statements of fact made by the Appellate Tribunal in the statement of a case. Our only jurisdiction is that, if in any case we are not satisfied that the statements contained in the statement of the case are sufficient to enable us to determine the question raised by it, we have power to send it back to the Appellate Tribunal for a second helping of facts. Here it is impossible to say that the facts as stated in the statement of the case were insufficient to have enabled the Income-tax Officer to conclude that the trust in this case was from the beginning, and is now, a public trust. That is sufficient to dispose of the matter upon the ground that this religious trust is not a private one at all but is a public one. Even if this had not been so, the findings of the Appellate Tribunal would still have been ample to show that the income of the trust, whether public or private, enures for the benefit of the public. For these reasons we answer the question put to us by saying that the assessee temple is a public religious trust, and, as such, is exempt from taxation in respect of the income derived from the trust in question by virtue of Section 4 (3) (i) of the Indian Income-tax Act.

The respondent assessee is entitled to his costs of this reference. We fix the fee of the learned counsel appearing for the department at two hundred rupees.

Reference answered accordingly.

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[IN THE NAGPUR HIGH COURT.]

INCOME-TAX APPELLATE TRIBUNAL, BOMBAY

v.

HAJI SABUMIYAN HAJI SIRAJUDDIN.

GRILLE, C.J., and SEN, J. December 8, 1944.

INDIAN INCOME-TAX ACT (XI OF 1922 AFTER AMENDMENT IN 1939), SEC. 10 (2) (xii)—BUSINESS EXPENDITURE—MONEY PAID TO COLLECT *Harra* AND LAC FROM FOREST TREES—WHETHER CAPITAL EXPENDITURE OR BUSINESS EXPENDITURE.

The assessee took leases of several forests for the right to take harra *nut and lac from the forest trees in consideration of certain sums payable in instalments spread over the contract period. Under the leases the assessee was permitted to pluck, sell, sub-let and remove from the forest the said produce and he was given possession of the trees within the entire area of the estate*:

Held, *that the payment in instalments to the owners of several forests was a capital expenditure and could not therefore be allowed as a deduction under Section 10 (2) (xii) of the Indian Income-tax Act.*

Golden Horse Shoe (New) Ltd. v. *Thurgood* (*[1934] 1 K.B. 548; 18 Tax Cas. 280*) and *Hakim Ram Prasad,* In re *[1936]* (*4 I.T.R. 104*) distinguished.

Cases referred to :—

Abdul Kayum Sahib Hussain *v.* Commissioner of Income-tax, Madras [1939] (7 I.T.R. 652).

Ahmedkhan Jamatkhan *v.* Mahammad Khan [1937] (A.I.R. 1937 Nag. 116; 169 I.C. 834; 9 R.N. 25).

Alianza Company Limited *v.* Bell ([1904] 2 K.B. 666; [1905] 1 K.B. 184; 74 L.J.K.B. 219; 92 L.T. 184; [1906] A.C. 18; 75 L.J.K.B. 44; 93 L.T. 705; 5 Tax Cas. 60; 5 Tax Cas. 172).

Anglo-Persian Oil Co. *v.* Dale ([1932] 1 K.B. 124; 100 L.J.K.B. 504; 145 L.T. 529; 47 T.L.R. 487; 16 Tax Cas. 253).

British Insulated and Helsby Cables Ltd. *v.* Atherton ([1926] A.C. 205; 95 L.J.K.B. 336; 134 L.T. 289; 42 T.L.R. 187; 10 Tax Cas. 155).

City of London Contract Corporation *v.* Styles [1887] (2 Tax Cas. 239; 4 T.L.R. 51).

Commissioner of Income-tax, Madras *v.* P. T. Chengalvaroya Chettiar [1937] (5 I.T.R. 70; I.L.R. 1937 Mad. 792; 167 I.C. 864; 1937 M.W.N. 511; 45 L.W. 184; A.I.R. 1937 Mad. 300; (1937) 1 M.L.J. 182; 10 I.T.C. 136).

Commissioner of Income-tax, Madras *v.* Chengalvaroya Mudaliar [1934] (I.L.R. 58 Mad. 1; 2 I.T.R. 395; A.I.R. 1934 Mad. 617 (2); 40 L.W. 469; 67 M.L.J. 350; 1934 M.W.N. 840; 152 I.C. 48; 7 I.T.C. 323).

Commissioner of Income-tax, Madras *v.* Manavedan Tirumalpad [1930] (I.L.R. 54 Mad. 21; A.I.R. 1930 Mad. 764; 126 I.C. 596; 4 I.T.C. 421).

Commissioner of Income-tax *v.* Tika Ram and Sons Ltd. [1937] (I.L.R. 1937 All. 908; 5 I.T.R. 544; 171 I.C. 547; A.I.R. 1937 All. 708).

Duppa *v.* Mayo (1669) 1 Wms. Saund. 275; 85 E.R. 336.

Golden Horse Shoe (New) Ltd. *v.* Thurgood ([1934] 1 K.B. 548; 150 L.T. 427; 103 L.J.K.B. 619; 18 Tax Cas. 280).

Hakim Ram Prasad, *In re* [1936] (4 I.T.R. 104; 9 I.T.C. 181).

Hancock *v.* General Reversionary and Investment Co. ([1919] 1 K.B. 25; 88 L.J.K.B. 248; 119 L.T. 737; 35 T.L.R. 11; 7 Tax Cas. 358).

Imam Ali *v.* Rani Priyawati Devi [1938] (I.L.R. [1938] Nag. 31).

Imperial Chemical Industries (India) Ltd., *In re* [1935] (I.L.R. 62 Cal. 87; 39 C.W.N. 70; 7 I.T.C. 414; 3 I.T.R. 21).

Income-tax Appellate Tribunal, New Delhi *v.* Central India Spinning, Weaving and Manufacturing Co., Ltd. [1943] (11 I.T.R. 266; I.L.R. 1943 Nag. 307).

John Smith and Son *v.* Moore ([1921] 2 A.C. 13; 58 Sc.L.R. 313; 90 L.J.P.C. 149; 125 L.T. 481; 37 T.L.R. 613; 12 Tax Cas. 266).

Kauri Timber Company Limited *v.* Commissioner of Taxes ([1913] A.C. 771).

Marshall *v.* Green (1875) 1 C.P.D. 35.

Mulji Sickka and Co. *v.* Nurmohammad [1939] (I.L.R. [1939] Nag. 432).

Narmadaprasad *v.* Narayan Singh [1939] (I.L.R. [1939] Nag. 81).

Parmanand *v.* Birkhu [1909] (5 Nag.L.R. 21).

Raja Bahadur Kamakshya Narain Singh *v.* Commissioner of Income-tax [1943] (70 I.A. 180; 11 I.T.R. 513; 22 Pat. 713; 210 I.C. 1; A.I.R. 1943 P.C. 153).

Raja Devi *v.* Mohammad Yaqub [1925] (I.L.R. 47 All. 738).

Shankar Shambhaji Gangla *v.* Commissioner of Income-tax, Bombay [1936] (9 I.T.C 350).

Smith *v.* Incorporated Council of Law Reporting for England and Wales ([1914] 3 K.B. 674; 83 L.J.K.B. 1721; 111 L.T. 848; 20 T.L.R. 588; 6 Tax Cas. 477).

Sonu *v.* Bhadaria [1922] (19 Nag. L.R. 186).

Stratford *v.* Mole and Lea: Oil Silkstone Collieries Ltd. *v.* Marsh [1941] (24 Tax Cas. 20).

Vallambrosa Rubber Co., Ltd. *v.* Farmer [1910] (5 Tax Cas. 529; [1910] Sess. Cas. 519; 47 Sc.L.R. 488).

Van Den Berghs Limited *v.* Clark ([1935] A.C. 431; 153 L.T. 171; 51 T.L.R. 393; 104 L.J.K.B. 345; 19 Tax Cas. 390; 3 I.T.R. (Eng. Cas.) 17).

Reference under Section 66 (1) of the Indian Income-tax Act (XI of 1922) by the Income-tax Appellate Tribunal, Bombay: Miscellaneous Civil Cases Nos. 55, 56 and 57 of 1943, and Miscellaneous Civil Cases Nos. 96 and 97 of 1942.

The following statement of case was submitted by the Income-tax Appellate Tribunal in Miscellaneous Civil Case No. 55 of 1943.

STATEMENT OF CASE.

"The assessee, Haji Sabumiyan Haji Sirajuddin, has made these two applications under Section 66 (1) of the Indian Income-tax (Amendment) Act, 1939. They are respectively marked Exhibits A and A-1 in the appended list of documents. The Commissioner of Income-tax, Central and United Provinces, has filed written answers which are, respectively, marked B and B-1.

2. In each application the assessee formulated four questions for reference to their Lordships, two being stated in paragraph 5 and the other two in paragraph 6 of each. At the hearing, however, the representative on his behalf expressly withdrew the second question in paragraph 5 and both the questions in paragraph 6, so that the only question that we are asked to refer is the first question in paragraph 5 of each. The question in each case is identical, and we therefore propose to make a consolidated reference.

3. The contest arises out of assessments made upon the applicant for the charge years 1939-40 and 1940-41, respectively. In each of these assessments he claimed an allowance in respect of instalments of what he called 'lease money' paid to the owners of several forests as consideration for the exclusive right to take *harra* nut and lac from the forest trees. There is no dispute as to the total amount paid by the assessee in each account year. The Income-tax Officer declined to admit the assessee's claim on the ground that the payment was a capital expenditure. On appeal, his view was upheld by the Appellate Assistant Commissioner. Copies of the Income-tax Officer's and the Appellate Assistant Commissioner's orders are marked C, D, E and F, respectively. On appeal to the Tribunal we agreed with the Appellate Assistant Commissioner in thinking that the expense claimed by the assessee was capital expenditure. A copy of our judgment is Exhibit G.

4. The material facts which are few and undisputed are stated in paragraph 3 of our judgment. Briefly speaking, the assessee takes up forests from their owners for a term of years for the collection of *harra* nut and lac from the trees during the contract period in consideration of a money payment. In terms of the agreements the payment is made in annual instalments spread over the contract period. The assessee calls these payments as 'lease money.'

5. The question arising from these facts is whether the payments are revenue expenditure. On a consideration of the facts and decided authorities on the point we came to the conclusion that the expenditure was of a capital nature. Our reasons are recorded in paragraphs 3, 4 and 5 of our judgment.

6. The question that the assessee asks us to refer is doubtless a question of law arising out of our appellate judgment. We accordingly submit it to their Lordships for their opinion. The question is :—

Question referred.—Whether, in the circumstances of those cases, the payments made by the assessee by way of annual instalments to the owners of the forests for the exclusive right to collect *harra* nut and lac from the forest trees during the contract periods was a revenue expenditure that could be allowed as a deduction under Section 10 (2) (xii) of the Indian Income-tax (Amendment) Act, 1939 ? "

Counsel in—

Miscellaneous Civil Case No. 55 of 1943.

R. B. D. N. Chaudhuri, for the Commissioner.

P. P. Deo with *M. Adhikari*, for the assessee.

Miscellaneous Civil Cases Nos. 96 of 1942, 97 of 1942 and 56 of 1943.

R. B. D. N. Chaudhuri, for the Commissioner.

V. V. Kelkar, for the assessee.

Miscellaneous Civil Case No. 57 of 1943.

R. B. D. N. Chaudhuri, for the Commissioner.

R. Kaushalendra Rao, for the assessee.

JUDGMENT.

(Judgment of the Court was delivered by Sen, J.)

This is a reference under Section 66 (1) of the Indian Income-tax Act, 1922, by the Appellate Tribunal, Bombay, at the instance of the assessee, Haji Sabumiyan Haji Sirajuddin of Dongargarh.

The reference arises out of assessment for two years 1939-40 and 1940-41. The assessee in each of the years claimed a deduction on account of instalments of lease money paid to the owners of several forests for the right to take *harra* nut and lac from the forest trees.

The assessee has included in the paper book the two agreements dated 6th April, 1938, and 6th April, 1939, executed by the Commissioner, Chhattisgarh Division, Raipur, representing the Court of Wards in favour of Haji Sarfuddin Yakinuddin. Both the documents purport to be "leases." The first is for a period of three years commencing from the 1st October, 1937, and ending with the 30th September, 1940. The consideration for the lease is Rs. 31,000 which was payable in 12 quarterly instalments of Rs. 2,583-5-4 each, the first instalment falling due on the 15th December, 1937. The lease was of *harra* produce from the entire forest area within the limits of Panabaras-*cum*-Aundhi Zamindari estate, tahsil Balod, district Drug. The estate consists of 205 villages which have been specified in the agreement. The lessee agreed to deposit 1/6th of the consideration money, namely, Rs. 5,166-10-8 as security which amount, if not forfeited, was to be set off against the last instalments of the lease money. Under clause 2 the lessor agreed to permit the lessee to pluck, sell, sub-let, remove from the said forest, the *harra* produce and the lessee undertook not to remove or sell any other kind of produce. The clause recites that the lessor has given possession of the trees within the entire area of the said estate for the purpose of plucking the *harra* fruits. Under clause 8 the lessee undertook to remove all *harra* to his own custody outside the said forest area within six months of the expiry of the period of the lease. The lessor was to allow the lessee, free of charge, grass and leaves for thatching, and wood for preparing temporary huts. Other clauses of the agreement are not material for the purpose of this reference and need not be stated.

The second agreement is for five years commencing from the 1st May, 1938, and ending with the 30th April, 1943. The consideration of the lease is Rs. 2,100 which was payable in 10 half-yearly equal instalments of Rs. 210 each, the first instalment falling due on the 15th March, 1938. The lease was for the propagation of lac on *palas* and other kinds of trees from the entire forest area within the limits of Panabaras-*cum*-Aundhi Zamindari estate. The clauses of this agreement are almost indentical with the previous agreement, the only difference being that in place of *harra*, lac has been mentioned and there are a few more clauses in this agreement which are not material for this reference.

The assessee claimed a deduction of the instalments which he had paid to the lessor in accordance with the terms of the two agreements. This claim was negatived by the Income-tax Officer on the 8th February, 1941, on the ground that it is an item of capital expenditure and is not a permissible item of deduction under Section 10 (2) (xii) of the Indian Income-tax Act, 1922.

The Appellate Assistant Commissioner of Income-tax, Nagpur, upheld the order on the 14th July, 1941, except for a slight variation with which we are not concerned. The Appellate Tribunal, Bombay Branch, affirmed on the 25th May, 1942, the order of the Appellate Assistant Commissioner of Income-tax, Nagpur.

The assessee applied to the Appellate Tribunal and suggested five questions for submission to the High Court for opinion.

At the hearing of the case the assessee abandoned four questions and only one question was left outstanding. The Appellate Tribunal has referred the following question for our decision :—

"Whether, in the circumstances of those cases, the payments made by the assessee by way of annual instalments to the owners of the forests for the exclusive right to collect *harra* nut and lac from the forest trees during the contract periods was a revenue expenditure that could be allowed as a deduction under Section 10 (2) (xii) of the Indian Income-tax (Amendment) Act, 1939 ?"

The solution of the question depends on the interpretation of Section 10 (2) (xii) of the Indian Income-tax Act, 1922, as amended by the Indian Income-tax (Amendment) Act (VII of 1939).

Section 6 of the Act specifies the heads of income chargeable to income-tax. Profits and gains of business have been specified as one of the heads of income chargeable to income-tax. Under Section 3 tax for a year is chargeable in respect of the total income of the previous year. Section 10 is in these terms :—

"(1) The tax shall be payable by an assessee under the head 'profits and gains of business......' in respect of the profits or gains of any business ...... carried on by him.

(2) Such profits or gains shall be computed after making the following allowances, namely :—

(xii) any expenditure (not being in the nature of capital expenditure or personal expenses of the assessee) laid out or expended wholly and exclusively for the purpose of such business......"

The expenditure claimed by the assessee was laid out or expended wholly and exclusively for the purpose of such business. This has not been disputed by the Income-tax authorities.

The clause (xii) prohibits a deduction which is in the nature of a capital expenditure. The question for decision in this reference is whether

the expenditure incurred by the assessee was in the nature of a capital expenditure.

This section may be compared with the provisions of the English Income Tax Act, 1918, which are given in Schedule D, rules 1 and 3 applicable to Cases I and II which deal with tax payable in respect of any trade etc., not contained in any other Schedule. Under rule 1 the tax is chargeable without any other deduction than is by the Act allowed. Rule 3 is in these terms:—

"In computing the amount of the profits or gains to be charged, no sum shall be deducted in respect of—

(a) any disbursements or expenses, not being money wholly and exclusively laid out or expended for the purposes of the trade......

(f) any capital withdrawn from, or any sum employed or intended to be employed as capital in such trade........."

In the Indian Income-tax Act allowance is given in one clause in positive terms while in the English Act prohibition of deduction is given in two clauses. Clause (f) of the English Act may be taken to be an amplification of the expression "capital expenditure" mentioned in Section 10 (2) (xii) of the Indian Income-tax Act. The two expressions are not in identical terms though they mean substantially the same thing.

The English Income Tax Act does not contain any express allowance or enumeration of deductions. Under the Act in determining whether a particular item may or may not be deducted from the profits it is necessary first to enquire whether the deduction is expressly prohibited by the Act and then, if it is not so prohibited to consider whether it is of such a nature that it is proper to be charged against the incomings in a computation of the balance of profits and gains for the year. The Indian Income-tax Act contains an express allowance or enumeration of deductions. In determining whether a particular item may or may not be deducted from the profits, it is necessary to inquire whether the deduction is expressly allowed.

The Indian Income-tax Act of 1922 is both in its general framework and its particular provisions different from the English Income Tax Acts, so that decisions upon English Acts are in general of no assistance in construing the Indian Act. But on some fundamental concepts reference may be to some extent usefully made to English decisions, in particular as to the meaning of the word "income": see *Raja Bahadur Kamakshya Narain Singh* v. *Commissioner of Income-tax*[1]. Similarly reference may usefully be made to English cases as to the meaning of the expression "capital expenditure."

The expression "capital expenditure" has not been defined either in the English or the Indian Income-tax Act. No precise, full and accurate

(1) (1943) 70 I.A. 180, at p. 188; 11 I.T.R. 513.

definition of the phrase is to be found in the cases. It is not possible to lay down any hard and fast rule or to enumerate any rigid or scientific principle which can be applied to determine whether a particular payment is in the nature of capital expenditure.

Various tests have been formulated in several cases in determining whether an expenditure is a capital expenditure or a revenue expenditure.

In *Vallambrosa Rubber Co., Ltd.* v. *Farmer*[1], Lord Dunedin as President suggested one test: that a capital expenditure is a thing that is going to be spent once and for all, and income expenditure is a thing that is going to recur every year. This is however not decisive in every case. Instances may be cited where payment, though made "once and for all" has been held to be a revenue and not a capital expenditure: *Smith* v. *Incorporated Council of Law Reporting for England and Wales*[2], *Hancock* v. *General Reversionary and Investment Co.*[3], *Anglo-Persian Oil Co.* v. *Dale*[4], and *In re Imperial Chemical Industries (India) Ltd.*[5]

Lord Cave in *British Insulated and Helsby Cables* v. *Atherton*[6], amplified the rule in the *Vallambrosa case*[1], and suggested another test:—

"When an expenditure is made, not only once and for all, but with a view to bringing into existence an asset or an advantage for the enduring benefit of a trade, I think that there is very good reason (in the absence of special circumstances leading to an opposite conclusion) for treating such an expenditure as properly attributable not to revenue but to capital."

This test was applied in *Income-tax Appellate Tribunal, New Delhi* v. *Central India Spinning, Weaving and Manufacturing Co., Ltd., The Empress Mills, Nagpur*[7].

The difficulty in determining whether a payment is in the nature of capital expenditure is illustrated in this case. Five noble and learned law Lords took part in the case; they differed in their opinions. Viscount Cave, L.C., Lord Atkinson and Lord Buckmaster held that it was in the nature of capital expenditure while Lord Carson and Lord Blanesburgh reached a contrary decision. Lord Haldane in *John Smith and Son* v. *Moore*[8], applied the test of circulating as contrasted with fixed capital, *i.e.*, whether the payment in the particular case was from fixed or circulating capital. This test was applied by Lord Hanworth in *Golden Horse Shoe (New), Ltd.* v. *Thurgood*[9]. It is however difficult to draw a line between fixed capital and circulating capital and Lord Macmillan in *Van Den Bergh's case*[10] observed that he had not found it very helpful.

(1) (1910) 5 Tax Cas. 529, at p. 536.
(2) [1914] 3 K.B. 674.
(3) [1919] 1 K.B. 25.
(4) [1932] 1 K.B. 124.
(5) [1935] I.L.R. 62 Cal. 87; 3 I.T.R. 21.
(6) [1926] A.C. 205, at p. 213.
(7) [1943] 11 I.T.R. 266; I.L.R. [1943] Nag. 307.
(8) [1921] 2 A.C. 13.
(9) [1934] 1 K.B. 548.
(10) [1935] A.C. 431, at p. 443; 3 I.T.R. Eng. Cas. 17.

Decided cases, however, are of great assistance in coming to a conclusion whether a payment in a particular case is in the nature of capital expenditure.

In *Alianza Company* v. *Bell*[1], the appellants, an English company, were the owners of land in Chile containing deposits of a substance called caliche, from which they extracted by a process of manufacture nitrates and iodine for the market. The decision was that in computing their profits for income-tax the appellants were not entitled to deduct any yearly sum to meet the exhaustion of the caliche. The law has been clearly and lucidly stated by Channell, J., at page 673 in these terms:—

"In the ordinary case, the cost of the material worked up in a manufactory is not a capital expenditure; it is a current expenditure, and does not become a capital expenditure merely because the material is provided by something like a forward contract, under which a person for the payment of a lump sum down secures a supply of the raw material for a period extending over several years.........The question.........is what is the nature of the adventure or concern which this particular company is carrying on. If it is merely a manufacturing business, then the procuring of the raw material would not be a capital expenditure. But if it is like the working of a particular mine or bed of brick earth, and converting the stuff worked into a marketable commodity, then the money paid for the prime cost of the stuff so dealt with is just as much capital as the money sunk in machinery or buildings.........This company must be treated as a company formed for the purpose of working and developing the bed of caliche. If it carried on a general business of purchasing and developing similar properties it is possible the matter might be otherwise; but here it is formed merely to work this particular bed, and consequently the money sunk in purchasing this bed is a capital and not a current expenditure. Then, if it is a capital expenditure, no allowance can be made in respect of it in estimating the profits......Any prudent person who carries on a business or gets an income from something, in which the capital is necessarily wasting, either by lapse of time, as in the case of a leasehold, or by reason of the using up of the material with which he starts as part of his capital, will provide for such a case by a sinking fund—by putting aside each year so much in order to meet the exhaustion of the capital. But, although it is a prudent course to adopt, any deduction in respect of it is not permitted by the Income Tax Acts."

The statement of the law was affirmed by the Court of Appeal in *Alianza Co.* v. *Bell*[2]. Collins, M.R., at page 193 quoted the observation of Bowen, L.J., in *City of London Contract Corporation* v. *Styles*[3].

(1) [1904] 2 K.B. 666.
(2) [1905] 1 K.B. 184.
(3) (1887) 2 Tax Cas. 239.

"You do not use it 'for the purpose of' your concern, which means, for the purpose of carrying on your concern, but you use it to acquire the concern."

This principle was applied and the deduction claimed by Alianza Company was disallowed.

The decision was upheld by the House of Lords in *Alianza Co., Ltd.* v. *Bell*[1]. Lord Robertson at page 19 stated: "There is no doubt whatever that the scheme of the enterprise of this company was to invest their capital in the acquisition of this property and then to proceed to work it as a mining concern." The decision of Channell, J., was approved by the Court of Appeal in *Golden Horse Shoe (New), Ltd.* v. *Thurgood*[2].

A reference may be made to the decision of the Privy Council in *Kauri Timber Co., Ltd.* v. *Commissioner of Taxes*[3]. The facts of the case were these. A company carried on in New Zealand the business of cutting, milling and selling timber, and for the purpose of that business it had acquired, upon its incorporation and from time to time subsequently, rights over freehold and leasehold bush lands bearing natural timber, in some cases by purchasing the lands and in other cases by purchasing the timber thereon with the right to remove the timber within a stated period. The question was whether under the Land and Income Assessment Act, 1908, the company was entitled to make a deduction from the gross proceeds of its business in respect of the value of the standing timber which it had cut in determining the profits for assessment for income purposes. The leases were for a period of 99 years and there was no obligation upon the company immediately to cut down and remove the timber. Lord Shaw at page 776 observed:—

"It appears to the Board that the present case involves no refinement of distinction; for the transaction under which these timber rights were acquired was not one under which a mere possession of goods by a contract of sale was given to the appellant company, but was one under which they obtained an interest in, and possession of, land. So long as the timber, at the option of the company, remained upon the soil, it derived its sustenance and nutriment from it. The additional growths became *ipso jure* the property of the company. All rights of possession necessary for working the business of cutting or even for preserving uninjured the standing and growing stock of timber were ceded under the leases. All this, together with the business facilities for removal and sale, was granted to the company, which became thereby invested with the possession of, and an interest in, the land."

At page 777:—"There can be no question that the cost of acquisition of this possession of, and interest in, land, and of the timber rights thereon, was just as plainly a capital on cost as if the land, with the timber upon it,

(1) [1906] A.C. 18. (2) [1934] 1 K.B. 548. (3) [1913] A.C. 771.

had been bought outright. And just as plainly it was not a proper accounting debit item as against revenue."

At page 778 a note by the learned editor in the first volume of Saunders' Reports, page 277c, is quoted :—

"The principle of these decisions appears to be this: that wherever at the time of the contract it is contemplated that the purchaser should derive a benefit from the further growth of the thing sold, from further vegetation and from the nutriment afforded by the land, the contract is to be considered as for the interest in land; but where the process of vegetation is over, or the parties agree that the thing sold shall be immediately withdrawn from the land, the land is to be considered as a mere warehouse of the thing sold and the contract is for goods."

The decision was that the company was not entitled in its assessment for income-tax to make any deduction from the gross proceeds of its business in respect of the value of the standing timber which it had cut.

The principles deducible from these two cases are of general application and are not dependent on the special provisions of any statute.

A reference may be made to *Stratford* v. *Mole and Lea*: *Old Silkstone Collieries, Ltd.* v. *Marsh*[1]. In the first case the agreement was to run for three years with an option of renewal and respondents purchased all the sand and gravel upon a certain parcel of land, paying therefor a fixed sum per ton of all sand and gravel removed. In the second case the appellant company purchased all the coal which it could actually sever from the soil or freehold and thereby convert into chattels personal from specified seams during the two years following; the agreement expressly stated that it was not a mining lease or licence nor the grant of a *profit a prendre* but a contract of the sale and purchase of goods. The observations in Saunders' Reports were applied and it was held that the agreement in each case granted a *profit a prendre* which was a "right, privilege or benefit in, over or derived from land" and that the payments under the agreements were not admissible deductions for income-tax purposes.

In *Commissioner of Income-tax, Madras* v. *Manavedan Tirumalpad*[2], the assessee had purchased a forest with trees growing thereon and that as the trees were cut down and carried away the capital was thereby decreased and he claimed exemption from the assessment of the profits derived from the sale of timber. The decision was that the amounts received by the owner of unassessed forest lands by the sale of timber trees thereon are income liable as such to income-tax.

In *Commissioner of Income-tax* v. *Chengalvaroya Mudaliar*[3], the assessee had the exclusive privilege for the excavation of lime shells for the period

(1) (1941) 24 Tax Cas. 20.
(2) (1930) I.L.R. 54 Mad. 21.
(3) (1934) I.L.R. 58 Mad. 1; 2 I.T.R. 395.

of three years for Rs. 27,750 payable in twelve quarterly instalments. The assessee claimed a deduction of Rs. 11,775 on two grounds, (i) that the sum was in part payment of Rs. 27,750 and was paid as rent and (ii) that Rs. 27,750 was really the purchase price of the shells lying upon and under the land which under the agreement was to be excavated.

As regards the first contention Beasley, C. J., at page 5 stated that the amount paid could not be regarded in any sense as rent and observed :—

"The fact that it is payable by instalments does not make it so. The total amount payable is first mentioned and the payment of that total amount is merely spread over a certain time."

Dealing with the second point at page 5 the learned Chief Justice observed:—

"In my view, the payment in question was not made in order to carry on an already existing business and to earn a profit out of it.........Any expenditure made thereafter would of course be deductible. But this was an initial expenditure without which the assessee could not even have begun winning the shells."

Both the contentions were negatived. The decision was that the assessee was not entitled to deduct the sum in computing the profits.

In *Commissioner of Income-tax* v. *P. T. Chengalvaroya Chettiar*[1], the assessee got exclusive right to excavate shells lying under Government property for three years for a payment of Rs. 30,450 payable by certain instalments and described in the instrument as regards Rs. 10,150 (being one-third of the amount stated) as "the annual lease amount." The decision in *Commissioner of Income-tax* v. *Chengalvaroya Mudaliar*[2] was applied and it was held that the sum was a capital expenditure and was not a permissible item of deduction.

In *Abdul Kayum Sahib Hussain* v. *Commissioner of Income-tax, Madras*[3], the assessee acquired the exclusive right, for a certain period, to collect chanks from chank beds belonging to a person and agreed to pay a certain amount in instalments in consideration for the grant of the right. The decision was that the amount paid in instalments was a capital expenditure and was therefore not an admissible deduction.

In *Shankar Shambhaji Gangla* v. *Commissioner of Income-tax, Bombay*[4], the assessee acquired the right to quarry a hill and sell stones therefrom for the period of 10 years from 1928—1938 and set apart Rs. 4,150 every year for sinking fund which with compound interest in 10 years would make up Rs. 50,000. He claimed a deduction of Rs. 4,150 in computing his profits for assessment for 1934-35 for income-tax purposes. The decision was that he was not entitled to deduct that sum. The judgment is of two lines but the decision can be supported on principle.

(1) [1937] 5 I.T.R. 70 ; I.L.R. [1937] Mad. 792.
(2) (1934) I.L.R. 58 Mad. 1 ; 2 I.T.R. 395.
(3) [1939] 7 I.T.R. 652.
(4) (1936) 9 I.T.C. 350.

In *Commissioner of Income-tax* v. *Tika Ram and Sons, Ltd.*[1], the assessee was a proprietor of a part of the property and a lessee of the rest. The earth used to be dug up and utilized for the purpose of bricks. He claimed a deduction of Rs. 2,500 under Section 10 (2) (ix) of the Indian Income-tax Act, 1922, before its amendment. This was disallowed. At page 909 it was stated :—

"If the company had been purchasing merely raw materials for the purpose of manufacturing bricks, it would certainly have been entitled to a deduction of the price of such materials from the total income realised by the sale of the bricks during the year. But the position here is not that of a company which is merely carrying on the business of manufacture by purchasing raw materials and converting such materials into marketable commodities."

At page 910 :—"The position seems to be more analogous to that of a company which is working a quarry or mine rather than to an ordinary manufacturer who purchases raw materials for the purpose of his manufacturing business."

The decision in the *Alianza Company case*[2] was applied and it was held that the assessee was not a purchaser of raw material but a person who had acquired certain rights in the land and the amount invested by him was a capital expenditure.

The learned counsel for the assessee relied on *Hakim Ram Prasad, In re*[3]. The decision is not helpful as there were no facts upon which the judges could come to any conclusion upon the matter.

The learned counsel also relied on the decision in *Golden Horse Shoe (New), Ltd.* v. *Thurgood*[4]. The company acquired a right to take away and re-treat very large dumps of residual deposits resulting from the working of a gold mine and called "tailings." These tailings were known to contain a certain amount of gold and by a new process of treatment some of this gold was recovered and sold. The question was whether the company was entitled to deduct from profits or gains the cost of tailings from which the profit was derived. Lord Hanworth, M.R., at page 560 observed :—

"It seems then that the company bought these dumps which were no longer in a natural but in an artificial condition which were in such a state that they would not have passed under a lease of 'beds opened, or unopened, or minerals '.........for the purpose of treating them as their stock in trade lying stored and ready to their hand, at a fair price of £1,22,750 and their intention was to use them up and make what they could of them by and after treatment. They had not to win them from the soil, they had been gotten already."

(1) [1937] 5 I.T.R. 544; I.L.R. [1937] All. 908.
(2) [1904] 2 K.B. 666.
(3) [1936] 4 I.T.R. 104.
(4) [1934] 1 K.B. 548.

At page 562 :—" The present facts seem to point to a manufacturing business applied to raw material already won and gotten." Romer, L.J., stated that the question had to be decided whether the dumps were to be regarded as fixed capital or as circulating capital, and recognised that it is not always easy to determine whether a particular asset belongs to the one category or the other. The determining factor, according to him, is the nature of the trade in which the asset is employed. At page 564, dealing with the case of mine : " the purchase of the mine is not a purchase of coal but a purchase of land with the right of extracting coal from it. The land is regarded merely as one of the means provided by the manufacturer for causing coal to be brought to his gas works, and therefore as much part of his fixed capital as would be any railway trucks or lorries provided by him for the same purpose."

After quoting the observations of Lord Sumner in *John Smith and Son* v. *Moore*[1], at page 38 : " The business carried on was not that of buying and selling contracts, but of buying and selling coals, and the contracts, which enabled the seller of the coals to acquire the coals, were no more the subject of his trading as a stock in trade for sale than a lease of a brickfield would be the subject of a sale of bricks."

At page 565 Romer, L. J., put the following question, " Are the dumps the raw material of the appellants' business or do they merely provide the means of obtaining that raw material ?" and answered that they were the raw material itself, and concluded the judgment by stating that it was a circulating capital. The decision in the case was that the amount expended in acquiring the tailings was in the nature of an expenditure on the raw material of the company's trade and that as such for the purpose of assessing the company's profits or gains the cost of the tailings treated during the period of assessment was a proper deduction from the proceeds realized by the sale of the gold extracted.

This case as well as Miscellaneous Civil Cases Nos. 56 of 1943, 96 of 1942, 97 of 1942 and 57 of 1943 were argued on the same day as the point involved in all these cases is common.

The learned counsel for the assessees strenuously contended that their cases were not governed by the principles deducible from *Alianza Company* v. *Bell*[2] affirmed in [1905] 1 K.B. 184 and [1906] A.C. 18, and *Kauri Timber Company, Limited* v. *Commissioner of Taxes*[3] and submitted that the principle enunciated in *Golden Horse Shoe (New), Ltd.* v. *Thurgood* [4] was applicable.

The argument was that the assessees merely purchased the raw material under the several agreements and that in computing the amounts of profits or gains for assessment for income-tax purposes, the price of the material purchased should be deducted.

(1) [1921] 2 A.C. 13. (2) [1904] 2 K.B. 666. (3) [1913] A.C. 771. (4) [1934] 1 K.B. 548.

The assessee Haji Sabumiyan Haji Sirajuddin acquired the right to the forest produce of *harra* nut and lac from the forest area within the limits of Panabaras-*cum*-Aundhi Zamindari estate consisting of 205 villages.

The assessee Sheodas Daga obtained the right to the forest produce consisting of *harra*, mahua etc., for a few years under the agreements dated the 21st August, 1928, and the 24th September, 1936.

The assessee Mohanlal Hargovind obtained the right to the *tendu* leaves from certain forests for a number of years.

The question is, what is the nature of the right which each of the assessees acquired under several contracts?

The terms "movable and immovable property" have been defined variously in different Acts for various purposes. Under the General Clauses Act, 1897, they have been defined in these terms:—

"3. (25) 'Immovable property' shall include land, benefits to arise out of land, and things attached to the earth, or permanently fastened to anything attached to the earth.

"3. (34) 'Movable property' shall mean property of every description, except immovable property."

Under the General Clauses Act growing crops will fall under the definition "immovable property."

Under Section 2 (13), Civil Procedure Code, "movable property" includes growing crops. Immovable property has not been defined in the Code. The definition of movable property must be limited to the Code, for under Section 3 (25) of the General Clauses Act, 1897, standing crops are immovable property. Movable property has been defined in Section 2 (9) of the Registration Act to include standing timber, growing crops and grass, fruit upon and juice in trees, and property of every other description, except immovable property. Immovable property has been defined in Section 2 (6) of the Act to include land, buildings, hereditary allowances, rights to ways etc., or any other benefit to arise out of land, and things attached to the earth or permanently fastened to anything which is attached to the earth, but not standing timber, growing crops, nor grass. The combined effect of these two definitions is that growing crops are movable property.

Under Section 3 of the Transfer of Property Act immovable property does not include standing timber, growing crops or grass. Movable property has not been defined in the Act.

The definition of "goods" in the Indian Sale of Goods Act is as follows:—

"2. (7) 'goods' means every kind of movable property other than actionable claims and money; and includes stock and shares, growing crops, grass, and things attached to or forming part of the land which are agreed to be severed before sale or under the contract of sale."

This definition may be compared with the definition in Section 62 (1) of the English Sale of Goods Act, 1893, which is as given below :—

"'Goods' include all chattels personal other than things in action and money, and in Scotland all corporeal movables except money. The term includes emblements, industrial growing crops, and things attached to or forming part of the land which are agreed to be severed before sale or under the contract of sale."

The definition of "goods" in the Indian Sale of Goods Act is wider than in the English Act. Under the Indian Act stocks and shares are included within the definition of goods. Under the Indian law all growing crops are included in the term while under the English law only "industrial growing crops" are included.

In the English law the question has arisen with respect to the provision of the Statute of Frauds (29 Car. 2, C. 3) and the Stamp Act, 1891. Section 4 enacts that no action shall be brought on any of the contracts specified in the section "unless the agreement upon which such action shall be brought or some memorandum or note thereof shall be in writing and signed by the party to be charged therewith or some other person thereunto by him lawfully authorized." One of the contracts enumerated therein is a contract for sale of lands, tenements, or hereditaments, or any interest in or concerning them. Another clause which is included is an agreement that is not to be performed within the space of one year from the making thereof. The questions have arisen whether sales of growing crops and the like were sales of an interest in lands within the 4th Section or of goods within the 17th. Section 17 applies to contracts for the sale of goods, wares, and merchandise. Under the section the necessity for writing does not exist when the value is under £10, and it may be dispensed with in contracts for larger sums, by proof of part acceptance or part payment by the buyer or by giving something to bind the bargain. A contract for sale under the later section is exempt from stamp duty under the Stamp Act, but under the former a stamp is required.

Under Section 4 of the English Sale of Goods Act, 1893, a contract for the sale of any goods of the value of ten pounds or upwards is not enforceable by action unless the buyer shall accept part of the goods so sold, and actually receive the same, or give something in earnest to bind the contract, or in part payment, or unless some note or memorandum in writing of the contract be made and signed by the party to be charged or his agent in that behalf. There is no such corresponding law in India.

The notes on the case of *Duppa* v. *Mayo*[1] by the learned editor Sir Edward Vaughan Williams in the first volume of Saunders' Reports

(1) (1669) 1 Wms. Saund. 275, at p. 277 ; 85 E.R. 336, at p. 343.

correctly summarised the English common law on the subject. These were further explained and applied in *Marshall* v. *Green*[1]. They have been subsequently modified by the definition contained in the English Sale of Goods Act which is in terms different from the definition given in the Indian Sale of Goods Act. They are thus of doubtful application so far as the Indian Acts are concerned.

The contention of the assessees was that the purchase was of forest produce and not a lease of immovable property. Reference was made to the executive instructions on the preparation of forest contract agreements in the Forest Manual contained in Volume II at page 107. They do not however bear out the contention advanced. The relevant observations are reproduced below :—

"......Their distinctive feature lies in the monopoly given to the contractor to extract all the forest produce specified in the contract in the area covered by the contract.

2. In the past such contracts have been called 'licences' or 'leases.' Both terms are inaccurate. A licence is merely a permission given to one person to enter on the land of another person and there to do something. It is not, strictly speaking, a right to enter on the second person's land to *take* anything. As soon as a licence confers a right to take anything it *becomes a licence coupled with a transfer of the property taken*, though it may still popularly be called a licence..............

The term 'lease' is equally inappropriate to a forest contract. A lease confers a right to enjoy a piece of immovable property, either in perpetuity or for a certain time. The lessee is entitled to almost unrestricted rights of enjoyment, and can usually exclude all others, even the owner himself.

3. A forest contract is neither a licence nor a lease. It is primarily a sale of forest produce, clearly indicated. The forest contractor is given the right to extract and remove, usually within a prescribed period, all the forest produce of a specified kind within a defined area of forest. It has an element of *monopoly* in so far as no one but the forest contractor may take any of the specified forest produce within the area; and to that extent it differs from a forest licence.................

4. It is clear that *a forest contract must be something more than a mere sale of forest produce.* A forest contractor's right would be of no value if he and his servants and agents were treated as trespassers whenever they entered the forest. *A forest contract*, therefore, *carries with it what is known as an 'accessory licence'* enabling the contractor and his servants and agents to enter the forest and to do all lawful acts required for the extraction and removal of the forest produce sold to him."

(1) (1875) 1 C. P. D. 35.

These executive instructions have not the binding force of law but they correctly represent the law on the point as it is in accord with the decision of the Divisional Bench in *Messrs. Mulji Sickka and Co.* v. *Nurmohammad*[1], and *Narmadaprasad* v. *Narayan Singh*[2]. The question in *Messrs. Mulji Sickka and Co.* v. *Nurmohammad*[1] was about the nature of the right which a person gets under a written agreement to enter upon land, collect and take away *tendu* leaves for making *bidis* over a period of years. The decision was that it was not a lease but an exclusive licence coupled with a grant amounting to a *profit a prendre* and that such an agreement fell within Section 17 (1) (b) of the Registration Act and required registration. At page 441 it is stated :—

"These 'leases' are not 'leases' of leaves or crops. That is, the subject-matter is not the sale or transfer of leaves or crops. The subject-matter is the transfer of a right. We have therefore to consider not what leaves or crops are, but what the right is.........

The so-called 'lease' here in question is a licence and a grant. As a licence, it is within the meaning of Section 52 of the Easements Act and it does not amount to an interest in property. But to it is added a grant, *viz.*, a grant permitting the grantee over a period of years to sever from the land certain things which are attached to the earth. A tree is attached to the earth and with it all its parts..............Are the leaves of a *tendu* tree excepted because they fall within the expression 'growing crops'? This does not arise for our present purpose for what was transferred was not a crop but a right to pick leaves.

Here the grant amounted to a *profit a prendre*. A *profit a prendre* is a right to take something off the land of another person......... It is an interest in land and, in England must, under the Statute of Frauds, be in writing. (See Law of Property Act, 1925, Section 53). If in gross, as here, it can be created for a term or in perpetuity and is a tenement: see Laws of England (Hailsham edition), Volume 11, page 386."

At page 443 :—"The right to collect leaves is till more clearly a right relating to 'a benefit to arise out of land'."

The conclusion is at page 442 :—"We are accordingly of the opinion that these 'leases' amounted to grants of immovable property within the definition contained in the General Clauses Act, Section 3 (25), and Section 2 (6) of the Registration Act, as relating to 'benefits to arise out of land' and as not being excluded by Section 3 of the Transfer of Property Act or Section 2 (9) of the Registration Act."

The case disapproved of the decision of Pollock, J., in *Ahmedkhan Jamatkhan* v. *Mohammad Khan*[3], and of the Allahabad High Court in

(1) I.L.R. [1939] Nag. 432.
(2) I.L.R. [1939] Nag. 81.
(3) (1937) A.I.R. 1937 Nag. 116.

Raja Devi v. *Muhammad Yaqub*[1], the cases on which the assessees relied in support of their argument.

The question in *Narmadaprasad* v. *Narayan Singh*[2] was one relating to registration of a document which related to timber. At page 83 it was observed :—

"But the decision does not turn upon the question whether *tendu* leaves form movable or immovable property. In determining whether a document has to be registered, one is concerned not with the object which the transaction relates to but with the rights which the instrument creates or declares. If the right in question amounts to a right, title or interest in immovable property, then the instrument.................. must be registered. The question here is: does this document create 'a right, title or interest.............. to or in immovable property?' If it does, then it requires registration under Section 17 (a) of the Indian Registration Act............

But it is not necessary to decide in this case whether a sale of standing timber amounts to a profit or whether it confers an interest in the property sold under the Sale of Goods Act, for whichever way the matter is viewed, the result is the same in this particular case because of the terms of the document under consideration. There is something more than a mere licence to enter in order to cut and remove ascertained timber sold and that *something more creates rights and interests in immovable property.*"

The principle in *Kauri Timber Company, Limited* v. *Commissioner of Taxes*[3], though based on the statement of the law contained in the notes on the case of *Duppa* v. *Mayo*[4] by the learned editor Sir Edward Vaughan Williams in the first volume of Saunders' Reports, p. 277c, deducible from the cases cited therein, is applicable as the view there taken is consistent with the law as stated in the decisions of the Divisional Bench in *Messrs. Mulji Sickka and Co.* v. *Nurmohammad*[5] and *Narmadaprasad* v. *Narayan Singh*[2].

The right to collect lac is a right relating to immovable property : see *Parmanand* v. *Birkhu*[6], *Sonu* v. *Bhadaria*[7] and *Imam Ali* v. *Rani Priyawati Devi*[8].

The right to collect *harra* fruit is a right to the immovable property as it relates to a benefit to arise out of land within the meaning of Section 3 (25) of the General Clauses Act.

The principles deducible from *Alianza Company* v. *Bell*[9] and *Kauri Timber Company Limited* v. *Commissioner of Taxes*[3] are applicable to the cases which have been referred to us for our opinions and not the principle enunciated in *Golden Horse Shoe (New), Ltd.* v. *Thurgood*[10].

(1) (1925) I.L.R. 47 All. 738.
(2) I.L.R. [1939] Nag. 81.
(3) [1913] A.C. 771.
(4) (1669) 1 Wms. Saund. 275, at p. 277 ; 85 E.R. 336, at p. 343.
(5) I.L.R. [1939] Nag. 432.
(6) (1909) 5 Nag. L.R. 21, at p. 23.
(7) (1922) 19 Nag. L.R. 186, at p. 188.
(8) I.L.R. [1938] Nag. 31.
(9) [1904] 2 K.B. 666.
(10) [1934] 1 K.B. 548.

The price paid by the assessee for acquiring the right is a capital expenditure and is not a permissible item of deduction under Section 10 (2) (xii) of the Indian Income-tax Act, 1922.

Our answer to the question is that the expenditure is not a revenue expenditure but a capital expenditure and as such it cannot be allowed as a deduction under Section 10 (2) (xii) of the Indian Income-tax Act.

The assessee shall bear the costs of this reference and pay the costs of the Commissioner of Income-tax. Counsel's fee Rs. 100.

Reference answered accordingly.

APPENDIX

The judgment of the High Court in Miscellaneous Civil Case No. 56 of 1943, dated the 8th December, 1944, was as follows ;—

MESSRS. SHEODAS DAGA, HARRA FIRM OF KHARIAR

v.

COMMISSIONER OF INCOME-TAX, U. P. & C. P.

This is a reference under Section 66 (1) of the Income-tax Act, 1922, at the instance of the assessee, Messrs. Sheodas Daga, Harra Firm of Khariar. The relevant facts which have led to the present reference are briefly these :—

The assessee claimed a deduction of Rs. 11,000 as a revenue expenditure in computing the profits and gains of the business for the assessment year 1940-41. The payment was made by the assessee under two contracts dated 21st August, 1928, and 24th September, 1936. Under the first contract Lal Artatran Deo Zamindar of Khariar Zamindari granted a 'lease' in favour of Seth Balkishan Ramkishan Nathani of Raipur for five years from 1st October, 1934, to 30th September, 1939, for Rs. 50,000 payable in 5 instalments of Rs. 10,000 each. Under the 'lease' the lessee was allowed to pluck, buy or remove the forest produce consisting of *harra, mohwa, toli,* wax, honey, gum, *chironji, baichendi* etc. The other 'lease' was executed by Ganeshsingh Gulalsingh Zamindar of Narra in favour of Sheodas Daga for a period of 10 years commencing from 1st January, 1930, to 1st January, 1940, for Rs. 10,000 payable in instalments. The assessee collected the produce and in the *harra* account the debits included Rs. 10,000 and Rs. 1,000 being the lease money paid for the contracts of Khariar and Narra Zamindaris.

The Income-tax Officer, Raipur, by the order dated 8th February, 1941, disallowed the item as a capital expenditure and not a permissible item of deduction. The Appellate Assistant Commissioner of Income-tax, Jubbulpore, by the order dated 15th July, 1941, affirmed the order of the Income-tax Officer. The Appellate Tribunal (Bombay Bench) by the judgment dated 8th June, 1942, found on a consideration of the deeds (i) that the assessee got

the right to collect the foliage of the ~~trees~~ and other produce, in addition to a right of access etc., and that such a right cannot be regarded as a lease of forest produce and the payment for acquiring such a right cannot be called rent and (ii) that the money paid for the jungles did not amount to the price of raw material or stock in trade as the assessee had acquired an interest in the land itself and affirmed the order passed by the Appellate Assistant Commissioner in appeal.

The assessee filed an application under Section 66 of the Indian Income-tax Act, 1922, before the Appellate Tribunal, Bombay Bench, on 19th August, 1942, for a statement of the case and reference to the High Court. He suggested three questions which arose for decision in the case. The Appellate Tribunal has given reasons for not referring those questions to us for our opinion and has formulated the question in these terms:—

"Whether, on a true construction of the two forest contracts, the applicant is entitled to a deduction of Rs. 11,000 (Rs. 10,000 plus Rs. 1,000) from his business income, either under Section 10 (2) (i) or 10 (2) (xii) of the Indian Income-tax (Amendment) Act, 1922?"

No objection has been taken by the assessee before us to the question as framed by the Appellate Tribunal.

The two deeds which embody the contracts are not before us and it is not possible for us to give our opinion, regarding the nature of interest created by these documents. We, however, presume that these contracts must be of the type which we have considered in Miscellaneous Civil Case No. 55 of 1943.*

For the reasons given in our judgment in Miscellaneous Civil Case No. 55 of 1943*, we hold that the applicant is not entitled to a deduction of Rs. 11,000 from his business income under Section 10 (2) (xii) of the Indian Income-tax Act, 1922.

Section 10 (2) (i) of the Act is in these terms:—

"Such profits or gains shall be computed after making the following allowances, namely:—

(i) any rent paid for the premises in which such business,......is carried on, provided that when any substantial part of the premises is used as a dwelling-house by the assessee, the allowance under this clause shall be such sum as the Income-tax Officer may determine having regard to the proportional annual value of the part so used."

The business is not carried on in such premises and no question of allowance under Section 10 (2) (i) can possibly arise. The clause has no application to this case.

We have already held that this does not amount to a lease of immovable property and the payments under the contracts are not rents.

* See page 447 *supra*.

The consideration of each contract is first settled and the amount is payable in certain instalments. The amount so payable is not rent.

Our answer to the question formulated is that the applicant is not entitled to a deduction of Rs. 11,000 from his business income either under Section 10 (2) (i) or 10 (2) (xii) of the Indian Income-tax Act, 1922.

The assessee shall bear the costs of this reference and pay the costs of the Commissioner of Income-tax. Counsel's fee Rs. 100.

Reference answered accordingly.

The judgment of the High Court in Miscellaneous Civil Case No. 96 of 1942, dated the 8th December, 1944, was as follows :—

MESSRS. SHEODAS DAGA & CO., RAIPUR

v.

COMMISSIONER OF INCOME-TAX, LUCKNOW.

This is an application under Section 66 (3) of the Income-tax Act, 1922, by the assessee Messrs. Sheodas Daga and Company requiring the Commissioner of Income-tax to state the case and refer it to the High Court.

The assessee claimed a deduction of Rs. 11,000 as a revenue expenditure in computing the profits and gains of the business for the assessment year 1939-40.

The payment was made by the assessee under two contracts dated 21st August, 1928, and 24th September, 1936. Under the first contract Lal Artatran Deo Zamindar of Khariar Zamindari granted a 'lease' in favour of Seth Balkishan Ramkishan Nathani of Raipur for five years from 1st October, 1934, to 30th September, 1939, for Rs. 50,000 payable in 5 instalments of Rs. 10,000 each. Under the 'lease' the lessee was allowed to pluck, buy, or remove the forest produce consisting of *harra, mohwa, toli,* wax, honey, gum, *chironji, baichendi* etc. The other lease was executed by Ganeshsingh Gulalsingh Zamindar of Narra in favour of Sheodas Daga for a period of 10 years commencing from 1st January, 1930, to 1st January, 1940, for Rs. 10,000 payable in instalments. The assessee collected the produce and in the *harra* account the debits included Rs. 10,000 and Rs. 1,000 being the lease money paid for the contracts of Khariar and Narra Zamindaris.

The Income-tax Officer, Raipur, by the order dated 13th March, 1940, disallowed the item as a capital expenditure and not a permissible item of deduction. The Appellate Assistant Commissioner of Income-tax, Jubbulpore, by the order dated 3rd September, 1940, affirmed the order of the Income-tax Officer. In the course of argument it was urged before the Appellate Assistant Commissioner that the income derived from the forest produce under the two deeds was an agricultural income and was exempt from assessment. This contention was negatived by the Appellate Assistant Commissioner. The Commissioner of Income-tax,

Central and United Provinces, by the order dated 27th December, 1941, declined to interfere with the assessment under Section 33 of the Income-tax Act and refused to refer the case to the High Court under Section 66 (2) of the Act as the points involved, according to him, were fully covered by authority and must inevitably be decided against the assessee. The application was accordingly dismissed. Against this order the assessee filed an application to the High Court on 27th June, 1942, calling upon the Commissioner of Income-tax to state the case and refer it to the High Court. On 27th July 1942, the Divisional Bench issued notice to the other side. The parties have been heard on the application. The points raised in this application were :—

(i) Whether the expenditure of Rs. 11,000 incurred by the assessee towards payments to the Khariar and Narra Zamindaris under the deeds dated 21st August, 1928, and 24th September, 1936, was a revenue expenditure and a permissible item of expenditure deduction under Section 10 (2) (xii) of the Income-tax Act, 1922 ?

(ii) Whether the income derived by the assessee from the forest produce was an agricultural income and exempt from assessment ?

The Appellate Assistant Commissioner of Income-tax and the Commissioner of Income-tax have discussed the question involved in point No. 2 and have given reasons for holding that the income derived by the assessee from the forest produce under the terms of the deeds is not an agricultural income and not exempt from assessment. The second point was not raised by the assessee before the Income-tax Officer and has not been pressed in argument before us and must be deemed to have been abandoned. We refrain from giving our opinion on the second point as it was never argued before us.

The question raised in point No. 1 is the only question which calls for decision and is the same as the one involved in Miscellaneous Civil Case No. 56 of 1943.* For the reasons given in our judgment in Miscellaneous Civil Case No. 56 of 1943* our answer to the question is, no. The application fails and is dismissed with costs. Counsel's fee Rs. 75.

Application dismissed.

The judgment of the High Court dated the 8th December, 1944, in Miscellaneous Civil Case No. 97 of 1942 was as follows :—

MESSRS. SHEODAS DAGA & CO., RAIPUR

v.

COMMISSIONER OF INCOME-TAX, LUCKNOW.

This is an application under Section 66 (3) of the Income-tax Act, 1922, by the assessee Messrs. Sheodas Daga and Co. (Harra firm), Rajim, requiring

* See page 465 *supra*.

the Commissioner of Income-tax to state the case and refer it to the High Court. The assessee claimed a deduction of Rs. 4,600 paid by him to the Zamindars of Binda-Nawagarh and Fingeshwar in determining the profits or gains of his business for the assessment year 1939-40. The assessee paid Rs. 3,500 to the Zamindar of Binda-Nawagarh and Rs. 1,100 to the Zamindar of Fingeshwar. The two Zamindars had given him an exclusive right to collect *harra*, wax etc., from the specified forest area and the zamindaris. He claimed this amount as a business expenditure. The claim was disallowed by the Income-tax Officer, Raipur, on 13th March, 1940, on the ground that it was a capital expenditure and not a permissible item of deduction. The Commissioner of Income-tax by the order dated 27th December, 1941, declined to interfere with the assessment under Section 33 of the Act and refused to refer the case to the High Court under Section 66 (2) of the Act, as, according to him, the point involved was fully covered by authority and must inevitably be decided against the assessee.

Before the Commissioner of Income-tax for the first time the question was raised that the income derived by the assessee from the forest produce under the terms of contract was an agricultural income and exempt from assessment. The Commissioner stated that the point could not be referred to the High Court under Section 66 (2) of the Act as it was not raised either before the Income-tax Officer or before the Appellate Assistant Commissioner in appeal.

The assessee filed an application on 27th June, 1942, under Section 66 (3) of the Income-tax Act, calling upon the Commissioner of Income-tax to state the case and refer it to the High Court. On 27th July, 1942, the Divisional Bench issued notice to the other side.

In the application the contention that the income derived by the assessee was an agricultural income and was exempt from assessment for income-tax purposes has been raised. This was, however, not raised before the Income-tax Officer or the Appellate Assistant Commissioner of Income-tax and cannot be decided in this case. The point was not pressed before us in the course of argument and must be deemed to have been abandoned by the assessee.

The only point that survives for consideration in this case is, whether the expenditure of Rs. 4,600 incurred by the assessee to the Zamindars under the lease was a revenue expenditure and a permissible item of deduction?

For the reasons given in our judgment in Miscellaneous Civil Case No. 56 of 1943* our answer to the question is, no.

The application fails and is dismissed with costs. Counsel's fee Rs. 75.

Application dismissed.

* See page 465 *supra*.

[IN THE NAGPUR HIGH COURT.]

INCOME-TAX APPELLATE TRIBUNAL, BOMBAY

v.

MANAGING TRUSTEE, SHRI RADHA MADHO TRUST, SAUGOR.

NIYOGI and BOSE, JJ. December 3, 1945.

INDIAN INCOME-TAX ACT (XI OF 1922 AFTER AMENDMENT IN 1939 BUT BEFORE AMENDMENT BY AMENDING ACT XXIII OF 1941), SECS. 4 (3) (ia), 41 (1), FIRST PROVISO & 66—TESTAMENTARY TRUST—TRUST FOR ERECTION OF TEMPLE—INCOME FROM TRUST INCLUDED BUSINESS INCOME—INCOME USED FOR TEMPLE, DHARMASHALA AND SADAVART—BENEFICIARIES, WHETHER JURIDICAL PERSONS—WHETHER INCOME FROM BUSINESS ASSESSABLE AT MAXIMUM RATE—REFERENCE UNDER SEC. 66—JURISDICTION OF HIGH COURT.

A testator, by his will, settled all his property upon trusts directing that a temple be erected and the annual income be utilised for the temple, a dharmashala and a sadavart. The trust income was derived from several sources including money and grain-lending business. It was admitted that this business was not a business carried on in the course of carrying out the primary purposes of the trust and the income was not exempt from taxation under Section 4 (3) (ia) of the Income-tax Act. In the assessment year 1940-41 the Income-tax authorities assessed to income-tax the income from business which amounted to Rs. 1,175 on March 11, 1941, at the maximum rate under the first proviso to Section 41 (1) of the Income-tax Act before its amendment by the Indian Income-tax (Amendment) Act (XXIII of 1941) on the ground that as the beneficiaries of the dharmashala and the sadavart were a fluctuating body of persons and therefore indeterminate, the trustees did not receive the income as a whole on behalf of any one person or a determinate body of persons :

Held, (*i*) *that the argument that the income was devoted to specified "objects" and not for the benefit of "persons" was fallacious since the objects could not be divorced from the persons; that the idol installed in a temple was a juridical person and that the beneficiaries connoted by the temple, the dharmashala and the sadavart were all persons in the juristic sense ;*

(*ii*) *that the beneficiaries were not a specific, fixed or limited body of persons but wholly indeterminate ;*

(*iii*) *that the income however was not liable to be assessed under the first proviso to Section 41 (1) as the substantive section itself did not apply to testamentary trusts on the date of the assessment.*

A deed is a non-testamentary instrument which is intended to come into operation immediately or at some time during the lifetime of the executant and it could not therefore be construed in a manner as to include a will.

The Amending Act (XXIII of 1941) which brought testamentary trusts within the provisions of Section 41 came into force only on November 26, 1941, and it was not retrospective.

The function of the High Court in cases referred to it under Section 66 of the Income-tax Act is advisory only and is confined to considering and answering the actual question referred to it.

Where therefore in a reference under Section 66 (1) the Appellate Tribunal did not refer a question of law on a point because the assessee accepted its findings on it, the High Court has no jurisdiction to deal with that point.

Commissioner of Income-tax, Madras v. *Venkatachalam Chettiar [1944] (12 I. T. R. 261)* followed.

Cases referred to :—

Charitable Gadodia Swadeshi Stores *v.* Commissioner of Income-tax [1944] (12 I.T.R. 385 ; A.I.R. 1944 Lah. 465 ; 217 I.C. 314).

Commissioner of Income-tax, Bihar and Orissa *v.* Maharajadhiraj Kameshwar Singh of Darbhanga [1933] (1 I.T.R. 94 ; 12 Pat. 318 ; 142 I.C. 437 ; A.I.R. 1933 P.C. 108 ; 60 I.A. 146; 6 I.T.C. 401).

Commissioner of Income-tax, Madras *v.* Venkatachalam Chettiar [1944] (12 I.T.R. 261 ; A.I.R. 1944 Mad. 567 ; 218 I.C. 492 ; [1944] 1 M.L.J. 496).

Gurmukh Singh *v.* Commissioner of Income-tax, Lahore [1944] (12 I.T.R. 393 ; A.I.R. 1944 Lah. 353 (2) ; 220 I.C. 339 ; I.L.R. [1945] Lah. 173).

Hanmantram Ramnath *v.* Commissioner of Income-tax, Bombay [1945] (13 I.T.R. 203 ; A.I.R. 1945 Bom. 345 ; 222 I.C. 19 ; 47 Bom. L.R. 183 ; I.L.R. [1945] Bom. 693).

Harendra Kumar *v.* Commissioner of Income-tax, Bengal [1944] (12 I.T.R. 68 ; A.I.R. 1944 Cal. 308 ; 220 I.C. 442).

Jai Dayal Madan Gopal, *In re* [1933] (1 I.T.R. 186 ; I.L.R. 54 All. 846 ; 143 I.C. 390 ; A.I.R. 1933 All. 77 ; 6 I.T.C. 226).

National Mutual Life Association of Australasia Ltd. *v.* Commissioner of Income-tax, Bombay [1936] (60 Bom. 248 ; 160 I.C. 1 ; A.I.R. 1936 P.C. 55 ; 70 M.L.J. 412 ; 38 Bom. L.R. 364 ; 4 I.T.R. 44 ; 9 I.T.C. 128 ; 63 I.A. 99 ; 40 C.W.N. 965).

Noperam Ram Gopal *v.* Commissioner of Income-tax, Bihar and Orissa [1942] (10 I.T.R. 288 ; A.I.R. 1943 Pat. 39 ; 204 I.C. 484).

Pramatha Nath Mullick *v.* Pradyumna Kumar Mullick [1925] (52 I.A. 245 ; 87 I.C. 305; A.I.R. 1925 P.C. 139 ; 27 Bom. L.R. 1064 ; 22 L.W. 492).

Prosunno Kumari Debya *v.* Golab Chand Baboo [1875] (2 I.A. 145 ; 14 Beng. L.R. 450 ; 3 Sar. 449).

Rajendra Narayan *v.* Commissioner of Income-tax, Bihar and Orissa [1940] (8 I.T.R. 495 ; 190 I.C. 1 ; A.I.R 1940 P.C. 158).

Seth Gangasagar, *In re* [1931] (I.L.R. 53 A. 451 ; A.I.R. 1931 All. 417 ; 132 I.C. 329 ; 5 I.T.C. 458).

Trustees Corporation Ltd. *v.* Commissioner of Income-tax, Bombay [1930] (54 Bom. 437 ; 123 I.C. 177 ; A.I.R. 1930 P.C. 151 ; 34 C.W.N. 709 ; 4 I.T.C. 378).

Vadilal Lallubhai Mehta *v.* Commissioner of Income-tax, Bombay [1935] (3 I.T.R. 152 ; 59 Bom. 405 ; A.I.R. 1935 Bom. 170 ; 37 Bom. L.R. 89 ; 157 I.C. 1097 ; 9 I.T.C. 90).

Reference under Section 66 (1) of the Indian Income-tax Act (XI of 1922) by the Income-tax Appellate Tribunal, Bombay : Miscellaneous Civil Case No. 49 of 1944.

STATEMENT OF CASE.

"This is a reference under Section 66 (1) of the Indian Income-tax Act and is submitted at the instance of the assessee who is the Managing Trustee of Shri Radha Madho Trust, Saugor, C. P. His application in this connection is marked Exhibit A in the appended list. He requires us to submit for their Lordships' opinion a question of law arising out of our judgment in his appeal, R. A. A. No. 22 (C. P.) of 1943-44. The Commissioner of Income-tax, U. P. and C. P. and Berar, by his written answer, Exhibit B, agrees that a question of law arises for reference.

2. The material undisputed facts are briefly these. In 1896, one Seth Naraindas Geda declared a trust by means of his will whereby he settled all his property upon certain trusts directing that the annual income should be utilised for the purposes of Shri Radha Madho Temple, a dharmashala, *i.e.*, place of shelter, and a sadavart, *i.e.*, alms house. The trustees appointed by the will constructed the dharmashala and established the sadavart. The temple and the dharmashala are open to all Hindus, while the sadavart feeds the poor irrespective of their caste or creed. The trust income is derived from agriculture, house property, ground rent and a money and grain-lending business which is carried on by the trustees. There is no dispute that all this income is devoted to religious and charitable purposes just indicated.

3. Up to the year 1939-40 the trust income from all the four sources used to be exempted from income-tax under Section 4 (3) (i) of the Indian Income-tax Act which enacts that income from property held in trust for a religious or charitable purpose shall not be included in the total income of a person. The Act came to be amended on 1st April, 1939, and one of the amendments was the insertion of clause (ia) in Section 4 (3) (i) which is to the effect that income from business shall be exempt from tax only if such business is carried on in the course of the carrying out of a primary purpose of the trust institution, or the work in connection with the business is mainly carried on by the beneficiaries of the institution.

4. In the first assessment that was made upon the assessee for the charge year 1939-40 the Income-tax Officer exempted the trust income from all the sources from taxation according to the previous practice. But in the charge year 1940-41, and while making the assessment for that year, the Income-tax Officer thought that his predecessor had committed an error of law in exempting the income, having regard to the newly inserted clause (ia) in Section 4 (3) (i) of the Act. He accordingly re-opened the assessment under Section 34 of the Act and made a re-assessment bringing the income from business to the tax.

5. In the assessment for 1940-41 the Income-tax Officer determined the trust income from grain and money-lending business at Rs. 1,175 and

similarly brought it to the tax. The amount of the income however fell below the maximum not chargeable to the tax in that year. But the Income-tax Officer charged it to the tax by applying the maximum rate under the first proviso to Section 41 (1) of the Indian Income-tax Act as amended in 1939.

6. The assessee appealed to the Appellate Assistant Commissioner from each of the two assessments, but failed. Thereafter, he took two appeals to the Appellate Tribunal, R.A.A. Nos. 23 and 22 (C.P.) of 1943-44, respectively, from the re-assessment for 1939-40 and the assessment for 1940-41.

7. We set aside the re-assessment for 1939-40 holding that a discovery of an error of law committed by an Income-tax Officer did not amount to "definite information" within the meaning of Section 34 of the Act to justify the re-opening of an assessment by another Income-tax Officer. In this connection we relied on *Commissioner of Income-tax* v. *Mahomed Yusuf Ismail*[1]. We dismissed the other appeal from the assessment for 1940-41.

8. This reference relates to the assessment for 1940-41 alone. But we have referred to the re-assessment for 1939-40 inasmuch as we consolidated the two appeals and recorded our main judgment in the appeal from that re-assessment. Copies of the assessment and the Appellate Assistant Commissioner's orders in connection with the assessment for 1940-41 are, respectively, Exhibits C and D and copies of our judgments in the two appeals to the Tribunal are Exhibits E and F.

9. As just stated this reference relates to the assessment for 1940-41 alone. The two points that the assessee raised in that appeal were :—

(i) That the trust income from business was exempt from taxation under Section 4 (3) (i) of the Act, and

(ii) that, at any rate, the amount of the income fell below the maximum not chargeable to the tax in the year of assessment, and that it was wrong to bring it to the tax by applying the maximum rate.

10. On both these points we held against the assessee. He has accepted our finding on the first point that the income from business is not exempt from taxation under Section 4 (3) (i) of the Act having regard to the amendment in that section by the insertion of clause (ia).

11. This reference is confined only to the second point. The Income-tax Officer determined the amount of tax by applying the maximum rate under the first proviso to Section 41 (1) of the Act. That proviso, too, was inserted in the Act of 1939, and is to the effect that where any income, profits or gains or any part thereof are not specifically receivable on behalf of any one person, or where the individual shares on whose behalf they are receivable are indeterminate or unknown, the tax shall be levied and

(1) [1944] 12 I.T.R. 8.

recoverable at the maximum rate. We held that this proviso applied to the trust income in question and our reasons are recorded in paragraph 4 of our judgment.

12. Being dissatisfied with our finding on the point the assessee requires us to submit the question to their Lordships which we do in the following form:—

Question referred.—Whether, in the circumstances of the case, the total income of Rs. 1,175 which is income from business carried on by the trustees has been properly charged to income-tax at the maximum rate in view of the proviso to Section 41 (1) of the Indian Income-tax Act, 1922, as amended in 1939?"

R. Kaushalendra Rao, for the applicant.

M. R. Bobde and *V. R. Sen*, for the opposite party.

JUDGMENT.

This case arises on a reference made by the Income-tax Appellate Tribunal under Section 66 (1) of the Indian Income-tax Act, 1922.

The facts are that in 1896 one Seth Narayandas Geda, by his will, settled all his property upon trusts directing that a temple be erected and the annual income be utilized for the temple, dharmashala (rest house) and sadavart (house for feeding or distributing charity to the poor).

The trust income is derived from several sources including money and grain-lending business. It was admitted that this business was not a business carried on in the course of carrying out the primary purposes of the trust and that the trust was not entitled to exemption from tax under clause (ia) of Section 4 (3) of the Income-tax Act. But it was contended that the income was not liable to be taxed at the maximum rate under the proviso to sub-section (1) of Section 41 of the Income-tax Act, 1922, for the reason that the income was devoted to the purposes of the temple of Shri Radha Madho, who, as a juridical person, was a known beneficiary. The Income-tax authorities, while conceding that the idol was the beneficiary, held that as the beneficiaries of the dharmashala and the sadavart were a fluctuating body of persons and therefore indeterminate, the trustees did not receive the income as a whole on behalf of any one person or a determinate body of persons, and rejected the contention. The Income-tax Appellate Tribunal heard the assessee's appeal on two points:—

(i) That the trust income was exempt from taxation under Section 4 (3) (i) of the Act.

(ii) That, at any rate, the amount of income fell below the maximum not chargeable to the tax in the year of the assessment (1940-41) and that the maximum rate was inapplicable.

The Tribunal overruled both these contentions. The assessee acquiesced in the Tribunal's decision on the first point but sought for reference of his case under Section 66 of the Act on the following question of law :—

Whether the first proviso to Section 41 (1) has been correctly applied in the circumstances or whether the entire income being less than the maximum not taxable is exempt from taxation ?

This question has been referred to us by the Tribunal in somewhat different words as follows :—

Whether, in the circumstances of the case, the total income of Rs. 1,175, which is income from business carried on by the trustees has been properly charged to income-tax at the maximum rate in view of the proviso to Section 41 (1) of the Indian Income-tax Act, 1922, as amended in 1939 ?

In this Court, the assessee has applied, relying on *Charitable Gadodia Swadeshi Stores* v. *Commissioner of Income-tax*[1], for permission to debate the point which he had conceded before the Tribunal, *viz.*, that the entire income of the trust is exempt from taxation even though trustees carried on business. This matter will be considered later.

The argument bearing on the question referred to this Court is two-fold :—

(a) that Section 41 (1) of the Income-tax Act has no applicability a there are no persons who can be said to be the beneficiaries although ther may be some specified objects for which the income is to be spent ;

(b) that in any case the proviso to Section 41 (1) is inapplicable a the total income is below the taxable limit.

There is no substance in the first branch of the contention for th obvious reason that the beneficiaries connoted by the temple, the dharm shala and the sadavart are all persons in the juristic sense. The idol insta led in a temple is a juridical person as was held by their Lordships of th Privy Council in *Prosunno Kumari Debya* v. *Golab Chand Baboo*[2] ar *Pramatha Nath Mullick* v. *Pradyumna Kumar Mullick*[3]. Not only ido but maths also are juridical persons : see Mulla's Hindu Law, Section 41

The argument that the income is devoted to specified "objects and not for the benefit of "persons" is fallacious since here the objects cann be divorced from the persons ; the worship of the idol or the maintenance the temple and the idol ; the dharmashala and the travellers seeking shel there ; and the sadavart and the poor people who receive food. These a so inextricably bound up together as to make it impossible to separate t objects from the persons. These persons become in the eye of law t *cestui que trusts*, *i.e.*, the persons for whom the trust exists. Obje

(1) [1944] 12 I.T.R. 385

(2) (1875) 2 I.A. 145.

(3) (1925) 52 I.A. 245.

without "persons" would be mere abstractions. What can reasonably be said is that beneficiaries are not a specific, fixed or limited body of persons but wholly indeterminate as are implied by the words, the travellers or the indigent: see *Harendra Kumar* v. *Commissioner of Income-tax, Bengal*[1].

It must therefore be held that Section 41 (1) of the Income-tax Act applies to the class of trustees to which the assessee belongs. But there is manifestly a difficulty in the application of the section as it stands to the assessee in the present case. The assessment was made by the Income-tax Officer on March 11, 1941, under the Amendment Act (VII of 1939) which came into force on April 1, 1939. On that date, the relevant part of the section as amended read as follows:—

"or any trustee or trustees appointed under a duly executed trust deed (including the trustee or trustees under any waqf deed which is valid under the Mussalman Waqf Validating Act, 1913) are entitled to receive on behalf of any person, the tax shall be levied upon and recoverable......"

Does the word "trust deed" apply to a testamentary instrument which creates a trust? The answer must be in the negative as will be presently shown.

Section 5 of the Indian Trusts Act provides that a trust can be created either by a non-testamentary instrument in writing "and registered, or by the will of the author of the trust." The non-testamentary instrument clearly signifies creation of the trust *inter vivos, viz.*, by the execution of a trust deed. A trust deed takes effect on registration, whereas a will takes effect on the death of the testator.

The word "deed" is defined in Halsbury's Laws of England (2nd Edition), Volume X, page 163. It is necessary for every transaction which the Common Law requires to be in writing (*ibid* page 168) and inasmuch as all declarations of trust respecting any land or any interest therein must be evidenced by writing (*ibid* page 239), it follows that such declarations of trust *inter vivos* must be made by a deed of trust. Delivery is essential for the deed to take effect (*ibid* page 197). What is essential to delivery of the document as a deed is that the party whose deed the document is expressed to be (having first sealed it) shall, by words and conduct, expressly or impliedly acknowledge his intention to be immediately and unconditionally bound by the provisions contained therein: see *ibid* page 198. It is thus evident that a deed is a non-testamentary instrument which is intended to come into operation immediately or at some time during the lifetime of the executant. It cannot, therefore, be construed in a manner as to include a will. It must, therefore, be held that the income of the trust under consideration was not liable to tax under Section 41 (1) of the Income-tax Act and that the action of the Income-tax authorities was *ultra vires*.

(1) [1944] 12 I.T.R. 68.

The legislature appears to have realised this defect which it removed by the Amending Act (XXIII of 1941) where the old wording of 1939 was substituted by the following :—

"or any trustee or trustees appointed under a trust declared by a duly executed instrument in writing whether testamentary or otherwise."

This Act No. XXIII of 1941 came into force on November 26, 1941. It does not purport to be retrospective and the assessment already made in this case before that Act came into force cannot be sustained. This was the view taken by the Madras High Court in *Commissioner of Income-tax, Madras* v. *Venkatachalam Chettiar* [1], with which we respectfully agree.

The learned Government Pleader contends that the testamentary character of the trust ceased with the death of the author of the trust and that the will was capable of being dealt with on the footing of a gift deed on the date of the assessment. The argument is specious but not sound. The very wording of the two Amending Acts of 1939 and 1941 makes it clear that the legislature conceived of two kinds of trust; one created by a trust deed and another by a testamentary instrument. The first of the two Amending Acts contemplated only those trusts which were created *inter vivos* and it cannot apply to those which were to come into effect after the death of the testator. Although the effect of the testamentary trust was at the time of the assessment the same as that of a trust deed, it cannot, strictly speaking, be regarded as identical with a trust deed for the purpose of Section 41 (1) of the Income-tax Act.

It is clear that the assessee was not liable to be assessed under the proviso to Section 41 (1) of the Income-tax Act as the substantive section itself did not apply to testamentary trusts on the date of the assessment.

That disposes of the reference. The assessee has raised a further point by an application for permission to contest the Appellate Tribunal's finding on the point of law that the trust income from business was not exempt from taxation under Section 4 (3) (i) of the Income-tax Act having regard to the amendment of that section by the insertion of clause (ia). The assessee had accepted that finding whether it was conceived as a point of law or otherwise, and in his application under Section 66 (1), he did not pray for the inclusion of that point in the reference by the Appellate Tribunal to this Court. The assessee invites our attention to the case published in *Charitable Gadodia Swadeshi Stores* v. *Commissioner of Income-tax* [2], as an authority for the proposition that the trust business such as the present is not covered by clause (ia). That may or may not be so. That is a question which arises on the merits. But before we go into the merits, we have to decide whether we have jurisdiction to deal with a point which is not referred to us. In the present case, we know that it was not referred

(1) [1944] 12 I.T.R. 261. (2) [1944] 12 I.T.R. 385.

to us because the assessee accepted the Tribunal's finding. We cannot admit any new question, even one of law, unless we are sure that we have power to act on our own motion to prevent what appears to us to be an illegality or injustice. But we think we have no such power. As pointed out by their Lordships of the Privy Council in *Rajendra Narayan* v. *Commissioner of Income-tax, Bihar and Orissa* [1], the function of the High Court in cases referred to it under Section 66 of the Income-tax Act is advisory only, and is confined to considering and answering the actual question referred to it: see also *Commissioner of Income-tax, Bihar and Orissa* v. *Maharajadhiraj Kameshwar Singh of Darbhanga* [2]; *Trustees Corporation Ltd.* v. *Commissioner of Income-tax, Bombay* [3]; *National Mutual Life Association of Australasia Ltd.* v. *Commissioner of Income-tax, Bombay Presidency and Aden* [4]; *Gurmukh Singh* v. *Commissioner of Income-tax, Lahore* [5]; *Noperam Ram Gopal* v. *Commissioner of Income-tax, Bihar and Orissa* [6] and *Hanmantram Ramnath* v. *Commissioner of Income-tax, Bombay* [7]. It is urged that the words in clause (5) of Section 66 of the Act, *viz.*, "case ...raised thereby" authorise this Court to raise any question of law *suo motu* for the purpose of deciding the case as a whole irrespective of whether any point of law is indicated in the reference or not. This contention also must be overruled in view of the clear exposition of that clause by the Judicial Committee in *Commissioner of Income-tax, Bihar and Orissa* v. *Maharajadhiraj Kameshwar Singh of Darbhanga* [8], in the following words:—

"The duty of the High Court under Section 66 (5) is to 'decide the questions of law raised' by the case referred to them by the Commissioner and it is for the Commissioner to state formally the questions which arise."

Our attention is invited to *Seth Gangasagar, In the matter of* [9], *Jai Dayal Madan Gopal, In the matter of* [10] and *Vadilal Lallubhai Mehta* v. *Commissioner of Income-tax, Bombay* [11], but these cases are not *ad rem* as the observations made in them were in respect of a reference made under Section 66 (2) of the Income-tax Act. They only lay down that when, on the mandamus issued by the High Court, the Appellate Tribunal states the facts of the case, but the issue or issues of law formulated by it are not clear or correct, it is open to the High Court to frame and decide the issue of law. The present case does not fall under Section 66 (2) of the Act. Here the Appellate Tribunal did not refer the case on the point because the assessee accepted its finding on it. The ways in which the question of

(1) (1940) A.I.R. 1940 P.C. 158, at p. 160; 8 I.T.R. 495, at p. 500;
(2) (1933) 12 Pat. 318; 1 I.T.R. 94.
(3) (1930) 54 Bom. 437.
(4) (1936) 60 Bom. 248; 4 I.T.R. 44.
(5) [1944] 12 I.T.R. 393.
(6) [1942] 10 I.T.R. 288.
(7) [1945] 13 I.T.R. 203.
(8) (1933) 12 Pat. 318, at p. 335; 1 I.T.R. 94, at p. 107
(9) (1931) 53 All. 451.
(10) (1933) 54 All. 846; 1 I.T.R. 186.
(11) (1935) 59 Bom. 405; 3 I.T.R. 152.

law is to be brought before the High Court are clearly prescribed by Section 66 read with Section 2 (10) and with the rules framed under Section 59 of the Act and no question of law, unless it comes before this Court in any of the modes prescribed by law, can be considered. We cannot, therefore, admit the question of law raised by the assessee in this Court.

The result is that we answer the reference in the negative by saying that the total income of Rs. 1,175 could not be charged at the maximum rate under the proviso to Section 41 (1) of the Act as that section as amended in 1939 did not affect the assessee.

The costs of the assessee will be paid by the Crown. Counsel's fees Rs. 50.

Reference answered in the negative.

[IN THE NAGPUR HIGH COURT.]

CENTRAL PROVINCES AND BERAR PROVINCIAL CO-OPERATIVE BANK LTD.

v.

COMMISSIONER OF INCOME-TAX, C. P. & U. P.

NIYOGI and BOSE, JJ. December 7, 1945.

INDIAN INCOME-TAX ACT (XI OF 1922), SEC. 8, PROVISOS 1 & 2—INTEREST ON SECURITIES—BANK—TAX-FREE AND TAXABLE SECURITIES—INTEREST ON CAPITAL BORROWED FOR INVESTING IN BOTH SECURITIES—WHETHER ALLOWABLE DEDUCTION—APPORTIONING OF INTEREST AND ALLOWING DEDUCTION OF IT IN RESPECT OF TAXABLE SECURITIES ONLY—LEGALITY—INTERPRETATION OF FISCAL STATUTES.

The assessee, a bank, had borrowed money for the purpose of investing in tax-free and taxable securities. The Income-tax Appellate Tribunal found that it was very difficult to allocate any particular borrowing to any particular investment:

Held, (*i*) *that in computing the income under Section 8 of the Income-tax Act, the department was not justified in splitting up and apportioning the interest on borrowed capital between the taxable and tax-free securities in proportion to the amount spent on the purchase of each kind of security and allowing deduction only in respect of the interest so apportioned to taxable securities;*

(*ii*) *that under the first proviso to Section 8 the whole of the interest on such part of the borrowed capital as was expended on the purchase of tax-free as well as taxable securities should be deducted;*

(*iii*) *that under the second proviso the whole of the interest receivable on the tax-free securities should be excluded in addition to the deduction in respect of the interest on borrowed capital.*

The Income-tax Act is a fiscal measure and as such many of its provisions are of necessity arbitrary. The duty of the High Court is to interpret the provisions of the Act and, if they are plain, to give effect to them regardless of the consequences; and if there is ambiguity, to construe the provision in favour of the subject even if it results in his obtaining a double advantage.

Commissioner of Income-tax, Madras v. *Madras Provincial Co-operative Bank Ltd.* [*1942*] (*10 I. T. R. 490*) dissented from.

Cases referred to :—

Commissioner of Income-tax, Madras *v.* Madras Provincial Co-operative Bank Ltd. [1942] (10 I.T.R. 490; A.I.R. 1943 Mad. 152; I.L.R. [1943] Mad. 390; 209 I.C. 33).

Hughes *v.* Bank of New Zealand ([1937] 1 K.B. 419; 106 L.J.K.B. 309; 156 L.T. 153; 6 I.T.R. 541; [1938] A.C. 366; 107 L.J.K. B. 306; 158 L.T. 463; 21 Tax Cas. 472; 6 I.T.R. 636).

Reference under Section 66 (1) of the Indian Income-tax Act (XI of 1922) by the Income-tax Appellate Tribunal, Bombay: Miscellaneous Civil Case No. 111 of 1943.

R. N. Padhye, for the applicant.

V. R. Sen, for the opposite party.

JUDGMENT.

This is a reference under Section 66 (1) of the Income-tax Act. The assessee is the Central Provinces and Berar Provincial Co-operative Bank Ltd. It has various sources of income, among them interest from tax-free securities and that from taxable securities. In the year in question the income from the former source was Rs. 1,25,596 and from the latter Rs. 1,64,672. In order to earn these two items of income the assessee was obliged to borrow money and had to pay interest on the money so borrowed. This interest amounted to Rs. 1,58,515. The Income-tax Tribunal holds as regards this that: "In the case of a bank it is very difficult to allocate any particular borrowing to any particular investment as the investments keep on changing from time to time."

We accept this as a finding of fact binding on us. The question is whether and how far the sum of Rs. 1,58,515 which is the money the bank spent to enable it to make the income set out above, can be taken into account in determining the taxable income of the bank.

The question at issue between the department and the assessee will be more easily appreciated if they are set out as algebraic formulae. Let A be the income from the tax-free securities and B the income from the taxable, and let X be the interest paid by the bank on the loans borrowed for the purchase of these securities.

The assessee claims that its income is A plus B. It claims that it is entitled to deduct X from this under proviso 1 to Section 8 and in addition

to deduct A under proviso 2. Therefore according to the assessee its taxable income is A plus B—X—A, that is to say, B—X.

The contention on behalf of the department is two-fold. In the first place, it says that as the assessee is not able to say which loan was borrowed for which security, it is not entitled to deduct any part of X because Section 8, read as a whole only permits deductions in respect of taxed securities when the borrowings can be ascribed specifically and with certainty to the purchase of the security. In the case of the other kind of security, namely the tax-free, no deductions are permissible because A is already excluded from the taxable income, and if something further is excluded it will give the assessee a double advantage.

The department contends further that if that argument does not hold good, then, though we do not know which particular loan was borrowed for which investment we do know that X was borrowed to enable both kinds of purchases to be made. Therefore, X can be apportioned between the two types of security in proportion to their values as X1 and X2. The taxable income then becomes B—X2. The interest on the tax-free securities A is excluded as also X1. This is what the department has done in the present case. It has split the Rs. 1,58,515 into Rs. 51,750 in respect of the tax-free securities and Rs. 1,06,765 in respect of the taxable.

The dispute centres around this Rs. 51,750 which we have termed X1. The assessee claims that this must be deducted from the taxable income, otherwise it is in effect being made to pay tax on a part of its tax-free interest.

We consider it idle to enquire whether the assessee obtains a "double advantage" upon this interpretation or that, or whether the Central Government stands to gain or lose. That is the wrong approach to the problem. The question of advantage or loss depends upon the rules, not the rules upon the outcome of the result, because we are not concerned here with abstract logic or the principles of pure reason. The Income-tax Act is a fiscal measure and as such many of its provisions are of necessity arbitrary, and in almost any set of arbitrary rules an advantage here or drawback there are almost certain to occur, nor indeed is there anything to prevent the legislature from desiring and prescribing for just such a result. Our duty is to interpret the provisions of the Act and, if they are plain, give effect to them regardless of the consequences; and if there is ambiguity to construe the provision in favour of the subject and this even if it results in his obtaining a "double advantage." That is how all fiscal enactments are to be construed.

The Act purports to tax income. But it has its own definition of income and its own rules for determining what heads of income shall be subject to tax. All income is not taxable—only those expressly so declared

So far as the present matter is concerned we can proceed at once to Section 6. According to it,

"Save as otherwise provided by this Act, the following heads of income, profits and gains, shall be chargeable to income-tax in the manner hereinafter appearing, namely :—

* * * *

(ii) Interest on securities."

Now it will be observed that this draws no distinction between different kinds of securities. Both the taxable and the tax-free are covered but they are not necessarily both taxable because the section says "save as otherwise provided by this Act" and "in the manner hereinafter appearing." We have, therefore, to see whether there is any saving provision in other parts of the Act and whether "the manner hereinafter appearing" effects any modification. Section 8 is the next relevant provision. It commences thus :—

"The tax shall be payable by an assessee under the head 'Interest on securities' in respect of the interest receivable by him on any security of the Central Government........."

Here again, it is to be noticed that no distinction is drawn between taxable and tax-free securities. Both are here declared to be subject to tax. But there are two provisos and the clause reproduced above must be read subject to them. Proviso 1 runs :—

"Provided that no income-tax shall be payable under this section by the assessee in respect of any sum deducted from such interest by way of commission by a banker realising such interest on behalf of the assessee or in respect of any interest payable on money borrowed for the purpose of investment in the securities by the assessee . . . . ."

The provision is cumbrous but is, we think, divided into two parts which we consider should be separated. The part relating to the present matter should, we think, read as follows :—

"Provided that no income-tax shall be payable under this section by the assessee . . . . in respect of any interest payable on money borrowed for the purpose of investment in *the* securities by the assessee."

Here again, it will be necessary to split this up for purposes of analysis. First, we will take the last clause which runs : "for the purpose of investment in *the* securities." What are these securities? Note the definite article. Obviously the provision relates to the securities specified in the body of Section 8 which says," the tax shall be payable by an assessee under the head 'Interest on securities"'. We have already examined this part of the Act and have shown that the "securities" referred to embrace both taxable and tax-free securities. Therefore, the proviso must refer to both. Next we turn to the earlier clause of the proviso : "No income-tax

shall be payable . . . . in respect of any interest payable on money borrowed" etc.

Now it is obvious that income-tax is not payable on sums which the assessee has to pay out to others. Such moneys are not "income, profits or gains." They are outgoings and not income. But the clause must have meaning and therefore there must be cases in which the legislature considers that an outgoing would in substance be taxable under the Act but for the provision here made however much it might appear otherwise on the surface. In our judgment the only way in which effect and meaning can be given to the proviso is by deducting these outgoings from the interest on the securities and taxing only so much of the remainder as is made taxable under the Act. Let us analyse this more closely. Take a simple case in which a man's only income is interest from taxable securities, say Rs. 2,500. Let us assume that in order to purchase these securities he has to borrow money and that on that money he pays Rs. 1,200 interest. Now that man's profit is only Rs. 1,300 and not Rs. 2,500. It is true he received Rs. 2,500 but he is obliged to pay out Rs. 1,200 to enable him to receive it. Therefore all he gains is Rs. 1,300. If he is taxed on Rs. 2,500 it means that he is taxed not only on the Rs. 1,300 which is his profit but also on the Rs. 1,200 which is an outgoing. Of course, there is nothing to prevent the legislature from directing that that should be done, but equally there is nothing to prevent it from relieving an assessee of this extra burden. It seems to us that the proviso is intended to exclude the outgoing Rs. 1,200 from tax. We cannot see how else any intelligible meaning can be assigned to it. We observe that that is the construction placed upon the proviso in *Commissioner of Income-tax, Madras* v. *Madras Provincial Co-operative Bank Ltd.*[1] Leach, C. J., observes :—

"In other words, the tax is only payable on the amount of interest received, less the interest which the assessee has to pay as the result of having borrowed to make the investment."

We also observe that that is the sense in which the department has construed this proviso. In the instructions issued at page 276 of the Income-tax Manual, 8th Edition, corrected up to 1st January, 1940, it is said :—

"When a bank or other concern engaged in business similar to that of a bank receives deposits on account of loans *in the course of its business* and invests the money so borrowed as occasion arises, the *entire* interest on such borrowings will be allowed as a deduction against its *entire* income *liable to tax* without attempting at allocation of the borrowed money to investments in tax-free and other securities."

These instructions have been overlooked in this case. It is true there are further instructions as to what should be done when "there is definite

(1) [1942] 10 I.T.R. 490, at p. 499.

proof (not mere inference) that a certain sum was specifically borrowed for the purpose of tax-free securities and has been so invested," but, as we showed at the outset of our order, there is no proof here. We have accepted as binding the decision of the Tribunal regarding the facts. Now we must not be understood as endorsing these further instructions. We refrain from expressing any opinion on them one way or the other because the circumstances which they envisage are not present in this case. Our decision is confined to a case where, as the Tribunal has observed, "it is very difficult to allocate any particular borrowing to any particular investment." The argument addressed to us on behalf of the Commissioner was that when the Rs. 2,500 which we find on the receipt side of our hypothetical assessee's budget is taxed, that does not amount to a taxing of the outgoing of Rs. 1,200. It merely means that the outgoing is ignored and the income of Rs. 2,500 alone is taxed. Of course the argument was not put in quite that way because we are dealing here with two kinds of securities, but that is what it amounts to when reduced to its simplest terms.

In order to follow the argument as it was put to us, it will be necessary to revert to our algebraic notation. The department split up the outgoing X into X1 and X2 and assigned X1 to the tax-free securities whose interest is represented by A and X2 to the other. The argument was that as only B — X2 is taxed, it cannot be said that X1 or any portion of X is taxed. That sounds plausible but a man whose income is being taxed does not want casuistry. He wants facts. He is the man who pays. He is the man who is hit, and no amount of argument will convince him that his income is other than A plus B — X, or to put it into figures, if A is Rs. 1,000 and B Rs. 1,500 and X Rs. 1,200 then his profit, that is to say, what is left over to him, is only Rs. 1,300. If he is told that Rs. 1,000 of this is tax-free, then, according to the lights of the ordinary man in the street, only Rs. 300 would be taxable and if he is made to pay tax upon more, it is no use telling him that neither his outgoings nor his tax-free securities are being taxed. He is the man with the coins in his hand and count them how you will, only Rs. 300 remains when Rs. 1,000 is excluded. The department, however, would split the Rs. 1,200 proportionately and assign Rs. 480 to the tax-free securities and Rs. 720 to the other, and after doing that they would tax Rs. 1,300 — Rs. 720, that is Rs. 580. Now, where does the remaining Rs. 280 come from? It can only come from two sources. Either it comes from a part of the outgoing X in which case a part of the outgoing is being taxed contrary to the Act which only purports to tax "income, profits and gains," and contrary to the first proviso to Section 8, or it comes from the Rs. 1,000 in which case a part of the tax-free interest is being subjected to tax. As we have said the first proviso to Section 8 must have some meaning. It cannot mean that an outgoing is not to be taxed because that is

obvious from the fact that the Act only purports to tax "income, profits and gains." It must, therefore, mean that unless care is taken to exclude certain outgoings the result will be that in reality they will be taxed, however much surface calculations and philosophical speculations may appear to indicate the contrary. We have endeavoured to explain how that can come about. In our opinion the first proviso directs a deduction of the outgoings X from the incomings A plus B. We say from A plus B because the proviso speaks of "*the* securities" and, as we have seen, "the securities" mean all kinds, the taxable as well as the tax-free. Therefore, up to that point there is no justification for treating the two differently, nor indeed was that seriously challenged. What the Commissioner contends is that the second proviso makes the difference. The second proviso runs:

"Provided further that no income-tax shall be payable on the interest receivable on any security of the Central Government issued or declared to be income-tax free."

The Commissioner contends that unless the first proviso is taken to refer to taxable securities only, there is an overlapping which will give the assessee a double advantage; therefore, the two must be construed in that sense. But as we have said that is putting the cart before the horse. There is no reason why the assessee should not get a double advantage if the Act can be so construed. If the language is plain, there is nothing more to be said. If it is ambiguous, then, being a fiscal enactment, it must be so construed because that is the construction which most favours the subject.

In our opinion, it can be so construed, and of the two constructions the one contended for by the assessee is the one which strains language least. We consider, therefore, that it should be so construed. The proviso is plain. It directs that no income-tax shall be payable on the interest receivable from this class of security. The only way of ensuring that no income-tax is charged on it either directly or indirectly is by excluding the interest wholly from the assessee's total income and that in our opinion holds good in the case of the first proviso too. We have explained at length how in reality an assessee would be paying tax on an outgoing unless it is wholly excluded from computation even though by a skilful jugglery with words and accounts it may appear otherwise; and we have pointed out that the legislature must have realised this too, otherwise it could not have used the language it has employed in proviso 1. On the face of it, it seems absurd to suggest that an outgoing is, or can be taxed. But the legislature obviously envisaged such a possibility, otherwise proviso 1 is meaningless. We have shown how the possibility can, in given circumstances, become a reality. The same analysis discloses that this could also happen in the case of tax-free securities unless the interest on them is wholly excluded. In our

opinion the provisos mean that both X and A are to be excluded from computation.

We can find no justification for the parctice of splitting up X as the department has done. We may in this regard look to Section 10 also, though in an Act of this kind the construction of one section does not necessarily assist in the elucidation of another. Under Section 10 tax is payable on the profits and gains of a business. Now if a dealer sells a motor car for Rs. 6,000 his profit on that transaction is not Rs. 6,000 but is the selling price less what he had to pay. If he had to pay Rs. 5,000 in order to purchase the car so that he could sell it for Rs. 6,000 his profit is clearly only Rs. 1,000. Therefore the outgoing of Rs. 5,000 has to be deducted from the incoming of Rs. 6,000. The same applies in the case of securities. If a man has to spend Rs. 1,200 in order to purchase a return of Rs. 2,500 his real income or profit is only Rs. 1,300, and that in our opinion is what proviso 1 to Section 8 recognises. Then Section 10 allows a further deduction in sub-section (2) (xii). The Act recognises that profits and gains cannot be fairly computed by simply deducting the purchase price of a commodity from its selling price. Other factors such as reasonable business expenses, the maintenance of an office, and so forth, must also be-taken into consideration. In Section 10 (2) (xii) the whole of this is excluded without any attempt to allocate it between one kind of transaction and another.

Say a man's business consists wholly of the buying and the selling of shares and securities. If this was conducted on a large enough scale, it would be necessary for him to maintain an office. Say among the transactions he conducts is the purchase of taxable and tax-free securities which he is either unable to dispose of in a given year of assessment or considers it prudent to retain awaiting a rise in the market. It would be absurd to say that the sum allowed on account of office expenditure would have to be apportioned simply because he happens to receive interest on these two types of securities in the course of his business. In our opinion, similar considerations obtain in the case of Section 8. Take another example. Agricultural income is exempt under Section 4 (3) (viii). But say a man's business is partly agricultural and partly commercial, the commercial end of it being mixed up with the agricultural. Say he runs one office and one staff to supervise both sections. Would he have to apportion the office expenses which are permissible as a good deduction under Section 10 (2) (xii) between the two kinds? We can hardly think that that would be the case.

Giving the best consideration we can to all these matters, we are of opinion that the two provisos to Section 8 are independent and that they deal with different things. In our judgment, deductions are to be made under both heads. Turning now to the cases cited,

There are two from England namely, *Hughes* v. *Bank of New Zealand*[1] and the House of Lords upholding this on appeal, *Hughes* v. *Bank of New Zealand*[2]. We doubt if much is to be gained by examining these cases, though the point involved was the same, because they turn upon a construction of the English Statute which is not quite the same as our Act. Still, so far as they go, the matter was decided against the Crown and the tax-payer was allowed to deduct the interest on tax-free securities as well as expenses which went towards the earning of it despite the fact that it gave the tax-payer a "double advantage." (See Lord Wright's judgment at page 449 of the 1937 report). This upholds our contention that there is no reason why the tax-payer should not get a double advantage if that can reasonably be spelled out of the enactment. And in so far as any principle is to be deduced, the following observation of Lord Thankerton in the House of Lords (page 374) is relevant. He says that the contention of the Crown (similar to its contention here) "would involve the very serious frustration of what the parties, taking the securities from time to time, might be assumed to have contemplated." And again at page 378, "If the policy of the Crown is otherwise, it is for them to rectify the ambiguities by amending legislation."

The latter remarks were made in connection with the noble Lord's criticism that "I find the language of the sub-rule (2) of rule 7 evasive and ambiguous; a slight alteration of the words could have clearly expressed either of the opposing constructions." That is also the position here, and, following the lead of the House of Lords, we consider it proper to resolve the ambiguity in favour of the tax-payer.

Then again at page 378 Lord Thankerton says, after pointing out that the interest on borrowed capital was a proper deduction: "It does not require the presence of a receipt on the credit side to justify the deduction of an expense." That, in our opinion, is also the case here. The two matters are separable and distinct. Counsel for the Commissioner relies on *Commissioner of Income-tax, Madras* v. *Madras Provincial Co-operative Bank Ltd.*[3], a decision of the Madras High Court. That ruling favours the contention of the department, but with the utmost respect we prefer our view. The learned Judges give no reasons and merely express it as their opinion that proviso 1 is intended to cover taxable securities only. For the reasons we have given, we do not think that is the case, and as we have said, if there is ambiguity the matter must be resolved in favour of the tax-payer. The question referred is:

"Whether on the facts of this case the assessee's income from interest from tax-free securities has been properly computed after deducting the

(1) [1937] 1 K.B. 419; 6 I.T.R. 541.

(2) [1938] A.C. 366; 6 I.T.R. 636.

(3) [1942] 10 I.T.R. 490.

proportionate interest on borrowed capital at Rs. 73,846 for the assessment year 1940-41 and Rs. 47,788 for the assessment year 1941-42 ?"

Our answer is that the income has not been properly computed. We are of opinion (1) that the splitting up of the interest on borrowed capital and apportioning it between the taxable and tax-free securities is not justified; (2) that under proviso 1 to Section 8 the whole of the interest on such part of the borrowed capital as was expended on the purchase of these securities should have been deducted; and (3) that under proviso 2 the whole of the interest on the tax-free securities should have been excluded in addition to the deduction in respect of interest on borrowed capital. The costs of this reference will be paid by the Crown. Counsel's fee Rs. 100.

Reference answered accordingly.

[IN THE CALCUTTA HIGH COURT.]

GENERAL FAMILY PENSION FUND

v.

COMMISSIONER OF INCOME-TAX, BENGAL

GENTLE and ORMOND, JJ. April 12, 1946.

INDIAN INCOME-TAX ACT (XI OF 1922 BEFORE AMENDMENT IN 1939), SECS. 8, 10 & 12—INDIAN INCOME-TAX RULES, R. 25—MUTUAL LIFE ASSURANCE COMPANY—INCOME FROM INVESTMENTS AND INCOME FROM MEMBERS' SUBSCRIPTIONS—PROFITS ASCERTAINED BY ACTUARIAL VALUATION—METHOD OF ASSESSMENT—PRINCIPLE OF "FAVOURABLE ATTRIBUTION"—WHETHER APPLICABLE.

The assessee, a mutual life assurance company limited by guarantee, was exempted from the provisions of the Indian Life Assurance Companies Act, 1912. The objects of the company were, inter alia, *to grant terminable pensions or annuities dependent on human life in favour of any subscriber to the funds of the company, to invest the moneys of the company not immediately required and to pay out of any of the company's funds all expenses of management. The company also derived income from Government securities and other investments and its profits were ascertained by means of quinquennial actuarial valuation. The Income-tax authorities conceded that the transactions between the company and its members were mutual dealings and that income-tax was not assessable upon the surplus of the members' subscriptions by virtue of the decision in* STYLES' CASE [1889] (14 App. Cas. 381). *The question was how the company should be assessed in respect of its income from Government securities and other investments for the year ending 31st December 1936 :*

Held, (*i*) *that the income, profits and gains of the company should be assessed under rule 25 of the Indian Income-tax Rules in the form then in force without reference to Section 8, 10 or 12*;

(*ii*) *that in applying rule 25, from the surplus so ascertained, the company was not at liberty to appropriate its non-mutual receipts, that is income from its investments, in the first instance against its expenditure and to charge any balance of expenditure against its mutual receipts, that is income from members' subscriptions*;

(*iii*) *that rule 25 applied to all Indian life assurance companies and the exemption of the company from the operation of the Indian Life Assurance Companies Act did not prevent the application of the rule to it*;

(*iv*) *that the company's investments and the income derived from them were part of its life assurance business*;

(*v*) *that in the case of an assessment under rule 25, the question of allocation or appropriation with regard to payment of management expenses could not arise.*

A mutual assurance company in respect of its mutual dealings does carry on business. The decision in STYLES' CASE [1889] (14 App. Cas. 381), *as explained by the Court of Appeal and in the House of Lords in* CORNISH'S CASE [1926] (12 Tax Cas. 841), *was not that there were no profits made by a mutual company out of transactions with its members but that there were no profits assessable to tax.*

ORMOND, J.—*The Income-tax Officer in applying rule 25 should adopt a system of proportion, by taking first one-fifth of the surplus shown (by a comparison of the two actuarial reports) which would give the figure for total annual profit if the assessee company had been a non-mutual insurance company and then taking some proportionate part of that figure so as to arrive at a proper figure as would represent the portion of taxable profit of the assessee company.*

The principle of favourable attribution as laid down in COMMISSIONERS OF INLAND REVENUE v. STERLING TRUST LTD. [1925] (12 Tax Cas. 868), LONDON COUNTY COUNCIL v. ATTORNEY-GENERAL ([1901] A.C. 26) *and* EDINBURGH LIFE ASSURANCE CO. v. LORD ADVOCATE ([1910] A.C. 143) *not applied.*

LIVERPOOL AND LONDON AND GLOBE INSURANCE COMPANY v. BENNETT ([1911] 2 K.B. 577; [1912] 2 K.B. 41; [1913] A.C. 610) *applied.*

Cases referred to:—

Arthur Average Association for British, Foreign and Colonial Ships, *In re* [1875] (10 Ch. App. 542; 44 L.J. Ch. 569; 32 L.T. 713; 23 W.R. 939).

Commissioner of Income-tax v. Shaw Wallace & Co. [1932] (59 I.A. 206; 136 I.C. 742; 34 Bom. L.R. 1033; 63 M.L.J. 124; A.I.R. 1932 P.C. 138; 5 I.T.C. 211).

Commissioners of Inland Revenue v. Cornish Mutual Assurance Co., Ltd. [1926] (12 Tax Cas. 841; [1926] A.C. 281; 95 L.J.K.B. 446; 134 L.T. 545; 42 T.L.R. 255; 1924 W.N. 295).

Commissioners of Inland Revenue v. Sneath ([1932] 2 K.B. 362; 48 T.L.R. 241; 101 L.J.K.B. 330; 146 L.T. 434; 17 Tax Cas. 149).

Commissioners of Inland Revenue *v.* Sterling Trust Ltd. [1925] (12 Tax Cas. 868).

Edinburgh Life Assurance Co. *v.* Lord Advocate ([1910] A.C. 143; 79 L.J.P.C. 41; 101 L.T. 826; 5 Tax Cas. 472).

Fenton's Trustee *v.* Inland Revenue Commissioners ([1936] 2 K.B. 59).

Gresham Life Assurance Society *v.* Styles ([1892] A C. 309; 62 L J.Q.B. 41; 67 L.T. 479; 41 W.R. 270; 2 Tax Cas. 633; 3 Tax Cas. 185).

Liverpool and London and Globe Insurance Company *v.* Bennett ([1911] 2 K.B. 577; [1912] 2 K.B. 41; [1913] A.C. 610; 82 L.J.K.B. 1221; 109 L.T. 483; 29 T.L.R. 787; 6 Tax Cas. 327).

London County Council *v.* Attorney-General ([1901] A.C. 26; 70 L.J.Q.B. 77; 83 L.T. 605; 49 W.R. 686; 4 Tax Cas. 265).

National Mutual Life Association of Australasia *v.* Commissioner of Income-tax, Bombay Presidency and Aden [1935] (63 I.A. 99; 4 I.T.R 44; 9 I.T.C. 128; 160 I.C. 1; 40 C.W.N. 965).

New York Life Insurance Company *v.* Styles [1889] (14 App. Cas. 381; 59 L.J.Q.B. 291; 61 L.T. 201; 2 Tax Cas. 460).

Padstow Total Loss and Collision Assurance Association, *In re* [1880] (20 Ch. D. 137; 15 L.J. Ch. 344; 45 L.T. 774; 30 W.R. 326).

Raja Bahadur Kamakshya Narain of Ramgarh *v.* Commissioner of Income-tax, Bihar and Orissa [1943] (70 I.A. 180; 22 Pat. 713; 210 I.C. 1; 1943 A.L.J. 493; 48 C.W.N. 59; A.I.R. 1943 P.C. 153; 11 I.T.R. 513).

Sankaralinga Nadar *v.* Commissioner of Income-tax, Madras [1930] (53 Mad. 420; A.I.R. 1930 Mad. 209; 58 M.L.J 260; 4 I.T.C. 226; 126 I.C. 273).

Smith *v.* Anderson [1882] (15 Ch. D. 247; 50 L.J. Ch. 39; 43 L.T. 329; 29 W.R. 21).

Reference under Section 66 (1) of the Indian Income-tax Act (XI of 1922) by the Income-tax Appellate Tribunal.

STATEMENT OF CASE.

"These references are made in respect of four applications made by the applicant, General Family Pension Fund, for referring certain questions of law for the opinion of the High Court at Calcutta. The said four applications could be divided into two sets. (1) 66 R. A. No. 9-Bengal of 1942-43 and (2) 66 R. A. No. 6-Bengal of 1942-43, ask for reference of questions arising out of the orders passed by the Tribunal in respect of appeals preferred to the Appellate Tribunal by the Income-tax Officer, District III, Calcutta, against the order of the Appellate Assistant Commissioner, Calcutta "B" Range, in respect of the appeals against the assessments for the years 1937-38 and 1938-39 respectively. The other two applications, 66 R.A. No. 7-Bengal of 1942-43 and 66 R. A. No. 8-Bengal of 1942-43, ask for reference of questions arising out of the order of the Appellate Tribunal passed in appeal against the appeals preferred by the applicant himself against the orders of the Appellant Assistant Commissioner in respect of assessments made for the years 1937-38 and 1938-39 respectively. The applicant has formulated the following three questions of law as arising out of the order of the Tribunal dated the 28th July, 1942, in respect of the appeals preferred before them against the assessments for the two years 1937-38 and 1938-39 by both the applicant and the Income-tax Officer:—

"(1) Whether the decisions of the Assistant Commissioner of Income-tax, Calcutta, for the years 1928-29 to 1935-36 are binding upon the Income-tax Officer upon the principles of res judicata or otherwise.

(2) Whether the income, profits and gains of the General Family Pension Fund for the year ending the 31st December, 1936, should be assessed under rule 25 of the Indian Income-tax Rules in the form then in force.

(3) If the answer to (2) is in the affirmative, whether in applying the said rule 25, from the surplus so ascertained the Fund is at liberty to appropriate its non-mutual receipts, that is income from its investments, in the first instance, against its expenditure and to charge any balance of expenditure against its mutual receipts, that is income from members' subscriptions, thus leaving a final balance of mutual receipts which are non-taxable under the authority of *Styles' case*?"

The Commissioner of Income-tax, Bengal, the respondent to these four applications has replied objecting to questions (1) and (3) raised in the applications Nos. 9 and 6 referred to above as they do not arise out of the order passed by the Tribunal in the appeals preferred by the Income-tax Officer, District III, Calcutta, in R. A. A. Nos. 76 and 77, Bengal of 1941-42 and agreeing that the three questions of law raised arise out of the order of this Tribunal in regard to the appeals preferred by the applicant himself in R. A. A. No. 83-Bengal of 1941-42 and R. A. A. No. 84-Bengal of 1941-42 respectively. Question No. 2 raised by the applicant is incidentally being referred to in the Appellate Tribunal's order passed in the appeals preferred by the applicant himself in R. A. A. Nos. 83 and 84-Bengal of 1941-42. The questions raised by the applicant therefore arise collectively out of the 4 orders of the Tribunal in the 4 appeals decided by them against which 4 applications have been made and the form of the reference drawn will be adopted for all the applications. For the sake of economy of papers and printing, one reference may be printed. The answer to this reference will govern the other references also as the questions are common.

2. Four appeals referred to above were before us for disposal and the conclusion we arrived in each case has been stated in each case. The facts of the case and the contentions of the parties may now be set out.

3. *Facts of the case.*—The applicant in this case is a mutual concern and is an incorporated association formed for the purpose of providing maintenance for the widows and children of those who subscribe to it. The objects for which the company has been formed are disclosed in the Articles of Association which was filed before the Income-tax Officer and the relevant extracts on which the applicant relies are mentioned in the annexure to this statement marked "A". It is common ground that the assessee has no shareholders and pays no dividends. The Articles of Association defines members as follows:—

"Every person shall be deemed to have agreed to become and to be a member of the company who is a subscriber to the General Family Pension Fund at the date of the adoption of these Articles and holds a subsisting

entrance certificate or who in pursuance of the regulations hereinafter contained may hereafter become a subscriber and hold an entrance certificate."

Only the business of life assurance (as defined by Section 2 (5) of the Indian Life Assurance Companies Act, 1912) has been carried on by the applicant. The assessee has always been treated as a life insurance company; and although exempted by special notification dated the 17th September, 1913, from compliance with the provisions of the Life Assurance Companies Act, 1912, is now amenable to the provisions of the Insurance Act, 1938. The Appellate Assistant Commissioner by his order dated the 20th July, 1934, set aside the assessments for the years 1928-29 to 1933-34 under Section 31 (3) (b) and directed that the assessee should be treated as a life insurance company and assessed in accordance with the provisions of rule 25. Subsequent to this by a further appellate order in respect of the assessment of the said years 1928-29 to 1933-34, the same Assistant Commissioner on the 28th August, 1937, held that in computing the income, profits and gains of the assessee the position of the assessee as a mutual society must be taken into account and the principles laid down in the *Styles' case*[1] and the *Edinburgh Life Assurance Company's case*[2] would apply. This decision of the Assistant Commissioner was given effect to in the assessments of the years 1928-29 to 1935-36.

4. Relevant extracts from the above appellate orders are set out in the Annexure hereto and marked "B".

5. In pursuance of the said decision of the Assistant Commissioner the assessee was duly re-assessed for the years 1928-29 to 1935-36, its income being computed at nil and refunds being granted in respect of tax deducted at source. Furthermore, for the assessment years 1936-37 and 1937-38 the assessee was also assessed as a life insurance company in accordance with the principles laid down in the above-said appellate orders.

6. In the assessment for the year 1938-39 however, the Income-tax Officer departed from the method of assessment laid down in the abovenamed appellate orders and assessed the assessee under Sections 8 and 12 of the Indian Income-tax Act upon its income derived from "interest on securities" and from "other sources" respectively. Futhermore, following upon a notice under Section 34 of the Act served on the assessee, the Income-tax Officer re-opened the assessment for 1937-38 and made a re-assessment for that year similarly under Sections 8 and 12.

7. Copies of the said assessment and re-assessment orders are annexed hereto and marked "C" and "D" respectively.

8. From these orders the assessee appealed to the Appellate Assistant Commissioner. By his appellate order, dated 23rd December, 1941, the

(1) [1889] 14 App. Cas. 381. (2) [1910] A.C. 143.

Appellate Assistant Commissioner, Mr. Goswami, set aside the said assessments and ordered the income of the assessee in respect of both the said years to be re-assessed under rule 25. But he further directed that the income derived from interest on securities should be separately assessed under Section 8 of the Indian Income-tax Act allowing only for bank charges for collection and that similarly the income from any investments other than those falling under Section 8 should be assessed separately under Section 12 allowing for proportionate expenses.

9. Being dissatisfied with the said appellate order, the assessee appealed to the Appellate Tribunal. A cross appeal was also filed against the said order by the Income-tax Officer, Companies District III, Calcutta. The grounds of appeal filed by the assessee and the Income-tax Officer are annexed hereto and respectively marked "E" and "F".

10. For the assessee it was contended before us that:—

(a) Either on the principle of res judicata or otherwise, the Income-tax Officer was bound by the earlier decisions of the Appellate Assistant Commissioner.

(b) In the circumstances of the case it was not competent to the Income-tax Officer to re-open the assessment for the year 1937-38 under Section 34 of the Act.

(c) The assessee was carrying on a business of life insurance notwithstanding the fact that it was a mutual concern and accordingly it ought to be assessed under rule 25.

(d) In so assessing its income, the principle of *Styles' case* should be applied and the surplus of mutual receipts should not be treated as income assessable to Indian income-tax.

(e) In accordance with the principles laid down in the *Edinburgh Life Assurance Company's case* [1] and *Attorney-General* v. *London County Council* [2], the assessee was entitled to set off its expenditure against any part of its receipts so that its expenditure would absorb all receipts except the balance of the mutual receipts which would be exempt from taxation.

(f) In the case of a life insurance business it was not permissible to dissect the income from investments from the other receipts of the business because the investment of its funds is an integral part of such a business.

(g) The rule 25 precludes any such dissection.

11. For the department it was contended:

(a) That the Income-tax Officer was not bound by the previous ruling of the Assistant Commissioner.

(1) [1910] A.C 143 ; 5 Tax Cas. 472. (2) [1910] A.C. 26.

(b) That the principles of assessment followed by the Income-tax Officer were correct.

(c) That the cases of *Edinburgh Life Assurance Company* and *Attorney-General* v. *London County Council* (*supra*) were not applicable.

12. By two orders of this Bench of the Appellate Tribunal the direction of the Appellate Assistant Commissioner to compute the assessee's income in respect of the two assessment years 1937-38 and 1938-39 on the basis of rule 25 was countermanded for the reasons stated in the orders in R. A. A. Nos. 76 and 77-Bengal of 1941-42. Question No. 2 raised by the applicant arises out of the said orders of the Tribunal.

13. By two orders of the Appellate Tribunal in R. A. A. Nos. 83 and 84-Bengal of 1941-42 the appeals of the applicant against the orders of the Appellate Assistant Commissioner in respect of the two assessments for the years 1937-38 and 1938-39 were dismissed.

14. Questions Nos. 1 and 3 arise out of the order of the Tribunal in these two cases.

15. Question No. 1 raised by the applicant is as follows :—

"(1) Whether the decisions of the Assistant Commissioner of Income-tax, Calcutta, for the years 1928-29 to 1935-36 are binding upon the Income-tax Officer upon the principles of res judicata or otherwise."

For the reasons stated therein we have held that they are not binding on the department.

16. Question No. 3 raised by the applicant is as follows :—

"(3) If the answer to (2) is in the affirmative, whether in applying the said rule 25, from the surplus so ascertained, the Fund is at liberty to appropriate its non-mutual receipts, that is income from its investments, in the first instance, against its expenditure and to charge any balance of expenditure against its mutual receipts, that is income from members' subscriptions, thus leaving a final balance of mutual receipts which are non-taxable under the authority of *Styles' case*?"

17. For the reasons in the order, it has been held that the ruling in the *Edinburgh case* cannot be applied to the applicant. Question No. 2 is also dealt with in these two orders incidentally. Therefore these 3 questions do arise out of the orders of the Tribunal and are referred to the High Court for their opinion :

"(1) Whether the decisions of the Assistant Commissioner of Income-tax, Calcutta, for the years 1928-29 to 1935-36 are binding upon the Income-tax Officer upon the principles of res judicata or otherwise.

(2) Whether the income, profits and gains of the General Family Pension Fund for the year ending the 31st December, 1936, should be assessed under rule 25 of the Indian Income-tax Rules in the form then in force.

(3) If the answer to (2) is in the affirmative, whether in applying the said rule 25, from the surplus so ascertained, the Fund is at liberty to appropriate its non-mutual receipts, that is income from its investments, in the first instance, against its expenditure and to charge any balance of expenditure against its mutual receipts, that is income from members' subscriptions, thus leaving a final balance of mutual receipts which are non-taxable under the authority of *Styles' case*?"

S. C. Isaacs, for the assessee.

S. K. Gupta and *J. C. Pal*, for the Commissioner.

JUDGMENT.

GENTLE, J.—The General Family Pension Fund was incorporated under the Indian Companies Act, 1882, on 17th August, 1906; it is a company limited by guarantee; it has no share capital and its members are confined to persons who are subscribers for grants of pensions and annuities and who hold entrance certificates; the liability of each member is limited to a nominal sum of Rs. 5; since it complied with the provisions of Section 26 of the above Act, a licence was granted by the Bengal Government permitting the company to be registered without the word "limited" being included in its name.

The objects of the company, as contained in its Memorandum of Association, *inter alia*, are:—

3. (a) To acquire and take over as a going concern and to carry on and conduct and continue the objects of an existing unincorporated association or institution called the General Family Pension Fund founded and formed for the purpose of carrying on any business that has for its objects the acquisition of gain within the meaning of Section 4 of the said Act (Indian Companies Act, 1882).

(b) To grant terminable pensions or annuities dependent on human life or any other event or contingency in favour of any subscriber and/or any nominee or nominees (within the categories therein mentioned) of a subscriber to the funds of the company.

(d) To grant invest and deal with the moneys of the company not immediately required.

(g) To pay out of any of the company's funds all expenses of management of the company's business and objects.

4. The income and property of the company whensoever derived shall be applied solely towards the promotion of the business and objects of the company as set forth in the Memorandum of Association and no portion thereof shall be paid or transferred directly by way of dividend or bonus or otherwise by way of profit to the members of the company. Provided that nothing therein contained shall prevent (i) payment of specified

salaries and wages and (ii).........granting to any member a pension or annuity.

It is conceded by the Commissioner of Income-tax that the company carried on the business of a life assurance company. The Indian Life Assurance Companies Act, 1912, applies to all persons or bodies of persons, whether corporate or incorporate, (therein referred to as life assurance companies), who carry on such business within British India except, *inter alia,* to any fund which the Governor-General in Council may, by notification, exempt from the operation of the Act. By Notification No. 7345-97 dated 13th September, 1913, the General Family Pension Fund was exempted from the operation of that Act. It is also conceded by the Commissioner that the transactions between the company and its members are mutual dealings and that income-tax is not assessable upon the surplus of the members' subscriptions; this concession was made in pursuance of the decision in *New York Life Insurance Company* v. *Styles*[1], the principles of which, it is admitted, apply in India. It is convenient hereafter to refer to the General Family Pension Fund as 'the Fund.'

This reference is concerned with the assessments for the years 1937-38 and 1938-39. Since they are in respect of years prior to the passing of the Indian Income-tax (Amendment) Act, 1939, the provisions of the Indian Income-tax Act, 1922 (hereinafter called 'the Act'), as enacted before the Amendment Act of 1939, will apply to this reference.

The questions referred for the opinion of this Court are :—

1. Whether the decisions of the Assistant Commissioner of Income-tax, Calcutta, for the years 1928-29 to 1935-36 are binding upon the Income-tax Officer upon the principles of res judicata or otherwise?

2. Whether the income, profits and gains of the General Family Pension Fund for the year ending the 31st December, 1936, should be assessed under rule 25 of the Indian Income-tax Rules in the form then in force?

3. If the answer to (2) is in the affirmative, whether in applying the said rule 25, from the surplus so ascertained, the Fund is at liberty to appropriate its non-mutual receipts, that is income from its investments, in the first instance, against its expenditure and to charge any balance of expenditure against its mutual receipts, that is income from members' subscriptions, thus leaving a final balance of mutual receipts which are non-taxable under the authority of *Styles' case*?

The Fund has considerable sums invested in Indian Government and similar securities and also some other investments, *e.g.*, banking, Indian Treasuries and sterling securities brought into British India. The assessment for the year 1937-38 was made with regard to the Fund's financial year ending on 31st December, 1936, and the other assessment relates to the next

(1) [1889] 14 App. Cas. 381.

financial year. Reference, in any detail, to the earlier year is alone necessary as the later year, except for some variations in amounts, is substantially the same. During 1936 the total investments amounted in value to Rs. 77 lakhs, approximately, of which the main portion was Indian Government and like securities; the investment income amounted to about Rs. 4,75,000 in respect of which, in most instances, income-tax was deducted at source; the other receipts, to use a neutral term, were from the members and amounted to a sum slightly in excess of Rs. 1 lakh, being their annual subscriptions for pensions and annuities; the Fund paid about Rs. 4,12,000 in pensions and annuities and about Rs. 66,000 for management expenses.

For many years, the profits of the Fund have been ascertained by means of quinquennial actuarial valuations. In the valuation for the quinquennium ending on 31st December, 1934, the estimated surplus was Rs. 4,23,681 which sum was the basis for ascertainment of the profits during the five years. During a considerable number of years, up to and including the first assessment for the year 1937-38, assessments for income-tax were based upon the average annual net profits disclosed by the last preceding quinquennial actuarial valuation with, possibly, some additions to which reference is unnecessary. In respect of the year 1937-38, the Income-tax Officer first made an assessment based upon the actuarial valuation; subsequently he served a notice upon the Fund under Section 34 of the Act, re-opened the assessment and re-assessed the Fund upon its income during the financial year ending 31st December, 1936, from Government securities (under Section 8) and from the other investments (under Section 12), allowing deductions only of banker's charges or commission (under Section 8) and a proportionate amount of management expenses commensurate with the amount of the other investment income to the total amount of the gross receipts, comprising subscriptions from members, interest upon Government securities and upon other investments. In the first assessment for the year 1937-38 the profits were assessed as 'nil' and a sum of about Rs. 70,000, representing income-tax deducted at source in respect of interest upon investments, was repayable. By the second assessment, Rs. 97,000 income-tax was due, which amount included the sum of about Rs. 70,000, above-mentioned, which had been refunded. The receipts from members were not included in this assessment and the only amount allowed for management expenses was Rs. 2,526 out of Rs. 66,000. Substantially, the difference between the two assessments is that the Fund was required, by the second assessment, to pay Rs. 27,000, in addition to tax upon the interest from investments, instead of being entitled, according to the first assessment, to a refund of Rs. 70,000. The assessment for the year 1938-39 was made by the same method as the second assessment for the previous year and by which the sum of Rs. 24,609

tax became payable, in addition to tax deducted at source in respect of the investment income. Prior to the second assessment for the year 1937-38 it would seem that the whole of the Fund's receipts were considered to appertain to its business of a mutual insurance company and that rule 25 of the Income-tax Rules, which was then in force, was applicable to the Fund. This rule provides that:

"In the case of Life Assurance Companies incorporated in British India whose profits are periodically ascertained by actuarial valuation, the income, profits and gains of the Life Assurance Business shall be the average annual net profits disclosed by the last preceding valuation, provided that any deductions made from the gross income in arriving at the actuarial valuation which are not admissible for the purpose of income-tax assessment, and any Indian income-tax deducted from or paid on income derived from investments before such income is received, shall be added to the net profits disclosed by the valuation."

After the first assessment for 1937-38 had been made by application of rule 25, the Income-tax department subsequently formed the opinion that the rule did not apply to the company and it should be assessed upon its actual income during the year preceding the year of assessment, namely, in respect of its financial year ending on 31st December, 1936. Since the income for that year had not been the subject of the first assessment, the view taken was that that income had not been assessed but had escaped assessment, and the provisions of Section 34 were attracted; notice was given under the section, and the second assessment was made. The correctness of the department's opinion and the validity of the second assessment is dependent upon the question whether rule 25 is applicable to the Fund. Further, the validity of the assessment for 1938-39 will also be dependent upon the same question; this assessment was made in respect of the financial year ending on 31st December, 1937.

Dr. Gupta, for the Commissioner of Income-tax, contended that an assessment upon a previous year's income is correct and that rule 25 is inapplicable to the Fund, upon the following grounds:—

1. The rule does not apply to a life assurance company which is exempted from the provisions of the Life Assurance Companies Act.

2. The rule does not apply to a mutual life assurance company since it does not make and is precluded from making profits upon its life assurance business.

3. The rule is not the sole method of computation of the income or profits of a life assurance company, and the provisions of Sections 8, 10 and 12 of the Act are not abrogated nor excluded by the rule.

4. Assuming the rule applies to a mutual life assurance company, the income or profits to be ascertained by its operation are those which are

solely and directly derived from its life assurance business and not those derived from its securities or investments which are not an integral part of the business of a life assurance company.

5. Since the principles in *Styles' case* apply to the Fund, by which receipts from its subscribers in respect of life assurance are not subject to assessment to income-tax, rule 25 has no application to the Fund.

After the Indian Income-tax (Amendment) Act, 1939, was passed, rule 25 ceased to be in force, and the profits and gains of life assurance businesses are now ascertained by application of the rules contained in the Schedule to the Act of 1922, added to it by the Amending Act; rule 9 of the rules in the schedule expressly provides that those rules apply to a mutual insurance company. Dr. Gupta argued that, since the new rules are expressly made applicable to a mutual company, upon which rule 25 is silent, it should be inferred that the rule was inapplicable to a mutual company. The provisions of a subsequent enactment are not a safe guide to ascertain the meaning and effect of a repealed earlier enactment dealing with the same subject matter. Although an earlier enactment may not expressly make its provisions applicable in a particular instance, it does not necessarily follow that the provisions do not apply because a later enactment dealing with the same subject matter, contains an express provision for applicability in that instance. To ascertain its effect, the earlier enactment must be construed by reference to its provisions and those of the statute in which it is contained and not by reference to the later enactment.

The exemption from the operation of the Indian Life Assurance Companies Act, it is argued, prevents the application of rule 25. The rule does not restrict its application to those companies which are subject to that Act nor make it inapplicable to companies which are exempted from the operation of the Act. If limited application was intended, language to that effect could have been used, but there is none. The non-applicability of the Act does not change the nature of the Fund's business, which is that of life assurance. In its terms the rule applies to all Indian life assurance companies and the exemption of the Fund from the operation of the Act does not prevent application of the rule to it.

The argument supporting the assessments is put in this way. Since the Fund is a mutual assurance company, it does not derive income or make profits out of insurance transactions with its members and receipts from those transactions and the income from investments cannot be ascertained by application of rule 25; the income from Government securities has to be assessed under Section 8, which permits only a deduction in respect of banker's commission upon realisation, no other allowance, *e.g.*, management expenses, can be made; hence, in the assessments under Section 8, only banker's commission is deducted, and no allowance is made of

any part of the management expenditure; the remaining income, by way of interest from the Fund's other investments, falls within Section 12, which permits a deduction being made of expenditure solely incurred to obtain that income, and an allowance is made of a proportionate amount of the management expenses ascertained by computing the amount which the income received under this head bears to the total income; the income from investments is not income, profits or gains of the Fund's business of insurance and therefore does not fall within Section 10 since it is not part of that business.

The assessments exclude the premium income, or subscriptions from the members. Substantially, the whole expenses of management are treated as attributable to the transactions with the members; the position adopted is that because of the non-assessability of the receipts from that source, no deduction for management expenses can be made, save for a small sum with respect to the investment income assessed under Section 12; in the assessment for the year 1937-38, a sum of Rs. 2,526 out of a total management expense of Rs. 66,036 and for the year 1937-38 a sum of Rs. 117 out of Rs. 69,781 have been allowed under that section.

The effect of rule 25 is that the income, profits and gains of a life insurance company shall be the average annual net profits disclosed by a periodical actuarial valuation when such company ascertains its profits by that method. The contention by the Commissioner is that the Fund must derive "profits" from its life assurance business as a condition precedent to the application of the provisions of the rule; if there are no "profits" from that business, the rule cannot be applied; the Fund is a mutual insurance company and the receipts from its members are mutual dealings, the excess of those receipts over expenditure is not "profits"; and since there are no profits, the condition precedent is not fulfilled and the rule is inapplicable.

Styles' case[1] is relied upon as having decided that the receipts, or the excess of receipts over expenditure, from members of a mutual life assurance company, are not income or profits. The question for decision in that case was whether income-tax was payable upon the surplus from those receipts, after discharging the expenses for which they were obtained from members. This is made clear by the opening words of the argument for the insurance company at page 387 of the report. In *Commissioners of Inland Revenue* v. *Cornish Mutual Assurance Co., Ltd.*[2], Pollock, M.R., at p. 852 and Warrington, L. J., at page 857, pointed out in the Court of Appeal that, in *Styles' case* the House of Lords was not called upon to decide whether the assurance company was trading with its members or whether the surplus was profits but whether the surplus was profits or gains within the meaning of the English Income Tax Act. At page 866, of the report in the House of

(1) [1889] 14 App. Cas. 381. (2) (1926) 12 Tax Cas. 841.

Lords, Viscount Cave, L.C., said: "The point to be decided by the House in that case (*Styles'*) was whether the company there concerned was carrying on a trade from which it derived profits which were subject to tax and the actual decision was there were no such profits." Lord Bramwell, at page 394 in *Styles' case*[1], said: "The appellants do not carry on a profession, trade, employment or vocation from which profits or gains arise or accrue within the meaning of the Income Tax Act." The contention by the Commissioner of Income-tax, in the present reference, depends mainly upon the observations of Lord Watson, at page 394 in *Styles' case*[1], that "when a number of individuals agree to contribute funds for a common purpose, such as the payment of annuities, or of capital sums, to some or all of them, on the occurrence of events certain or uncertain and stipulate that their contributions, so far as not required for that purpose, shall be repaid to them, I cannot conceive why they should be regarded as traders, or why contributions returned to them should be regarded as profits." With respect to these observations Pollock, M.R., said, in the Court of Appeal, in *Cornish's case*[2], at page 853: "It is quite true that Lord Watson and Lord Herschell refer to the question of whether the association were or were not trading." The Master of the Rolls then cited part of the observations by Lord Watson which I have quoted, and continued: "It is said that we ought to take note that those two noble Lords expressed the opinion that a mutual association, a body of persons associated together for the purpose of mutual insurance, do not carry on a trade, but it is to be observed that that is not the basis of the decision and both those noble Lords, when they are dealing with the question of trading, refer to it incidentally in order to arrive at whether or not the profits or gains, which are the result of that, are subject to income-tax. Thay do not refer to the question of trading *per se* and alone, but only to the question of trading incidental to the question which they had to decide, namely, whether the surplus was subject to income-tax." With respect to Lord Watson's observations Viscount Cave said, at page 867 of the report in the House of Lords in *Cornish's case*, that "I cannot help thinking that the very learned Lord directed his observations only to the real question before the House, namely, whether there were taxable profits within the Income Tax Acts."

Two earlier decisions, by the Court of Appeal, were not cited to, and were not considered by, the House of Lords in *Styles' case* but they were quoted with approval by Pollock, M.R., in the Court of Appeal and by Lord Cave in the House of Lords, in *Cornish's case*. *Arthur Average Association for British and Colonial Ships*[3] and *Padstow Total Loss and Collision Assurance Association*[4] concerned mutual marine assurance associations,

(1) [1889] 14 App. Cas 381.
(2) (1926) 12 Tax Cas. 841.
(3) [1875] 10 Ch. App. 542.
(4) [1880] 20 Ch. D. 137.

in which the opinions were expressed that each such association carried on the business of marine insurance and carried it on for the purpose of gain for itself or for its individual members. In *Cornish's case,* Viscount Cave referred to the *Arthur Average* and *Padstow cases* as supporting the view, which he expressed, that whilst a mutual assurance company only carries on business with its members, yet as every person who chose to effect a policy with the company *ispo facto* became a member, the restriction did not appear to prevent the transactions of the company from being business transactions. In *Cornish's case* it was held that a mutual assurance company carried on business and was assessable to Corporation Profits Tax imposed by the English Finance Act, 1920; Section 52 (2) of that Statute enacted that the profits to which the tax was applicable were the profits of a British company carrying on any trade or business; and, by Section 53 (2) profits should be the profits and gains determined on the same principles as those on which profits and gains of a trade would be determined for the purposes of Schedule D of the Income Tax Acts, provided that profits should include, in the case of mutual trading concerns, the surplus arising from transactions with members. The decision in *Cornish's case* that a mutual insurance company carried on business is conceded in the present reference, but the opinions expressed in the Court of Appeal and in the House of Lords in that case, regarding Lord Watson's observation in *Styles' case* with respect to a mutual assurance company, explain the length to which that noble Lords' observations should be considered as extending.

It was argued by Dr. Gupta that decisions of the English Courts upon the English Income Tax Acts are not usually of assistance to construe the Indian Act. In this connection the observations by the Board in *Raja Bahadur Kamakshya Narain of Ramgarh* v. *Commissioner of Income-tax, Bihar and Orissa*[1], are in point. When delivering the judgment of their Lordships of the Judicial Committee, Lord Wright said, at page 188: "The Indian Income-tax Act, 1922, which was a consolidating Act, is both in its general framework and its particular provisions different from the English Income Tax Acts, so that decisions on the English Acts are, in general of no assistance in construing the Indian Acts. But in some fundamental concepts reference may be to some extent usefully made to English decisions, in particular as to the meaning of the word 'income'". I venture to include the words "profits" and "gains" as being included in the effect of the above observation.

In the present reference the Fund is a mutual company which, it is admitted, carries on the business of life insurance, the transactions of insurance are effected between the Fund and its members from whom the

(1) (1943) 70 I.A. 180; 11 I T.R. 513.

Fund obtains receipts with respect to those business transactions. The Concise Oxford Dictionary defines income as "periodical receipts from one's business." In the judgment of the Board in *Commissioner of Income-tax* v. *Shaw Wallace and Company*[1], it is stated at page 212 that "'income,' their Lordships think, in the Act (the Indian Income-tax Act, 1922) connotes a periodical monetary return coming in with some sort of regularity, or expected regularity, from definite sources." The annual payments by the members to the Fund are covered by the above observation. Whilst, as its Memorandum of Association provides, the income of the Fund shall be applied solely towards the promotion and objects of the company and no portion shall be paid direct to its members, I am unable to see that there cannot be profits upon the transactions between the Fund and its members or that there is no income derived by the Fund from its business. At page 212 in *Shaw Wallace's case*[1], it was observed that the Act does not define "income" but expands it into "income, profits and gains"; this expansion is a matter of words and not of substance. The decision in *Styles' case* as explained by the Court of Appeal and in the House of Lords in *Cornish's case*, was not that there were no profits made by a mutual company out of transactions with its members but that there were no profits assessable to tax. The particular facts in *Styles' case* were that the balance of the receipts from members not required and used for the purpose for which those moneys were subscribed, was returned to the members; but, it is conceded in the present reference, although there is no direct return of the unused part of the members' subscriptions, the transactions are mutual dealings and, as such, those receipts, or the surplus from them, are not taxable. *Styles' case*, as explained by *Cornish's case*, is not an authority that a mutual company does not make profits out of transactions with members, the decision was that profits from those transactions are not assessable to tax by reason that, in effect, they arise out of transactions with itself. In my opinion, since the transactions between a mutual insurance company and its members arise out of the business which it carries on, any surplus therefrom is income or profits and a surplus from members' subscriptions is income and profits, but, by reason of the nature of the receipts being mutual dealings, such income and profits are not assessable to income-tax. Since that Fund derives profits from its insurance business which are ascertained by periodical actuarial valuation, it follows that rule 25 applies to the Fund.

Now as to the contention that rule 25 is not the sole method of computation of the income, profits and gains of a life assurance company and that Sections 8, 10 and 12 of the Act are not excluded nor abrogated by the rule. This argument appears to suggest that the department can ignore

(1) (1932) 59 I.A. 206.

the rule and utilise the above, and other, sections when it suits them or when they wish to do so. By Section 3, tax shall be charged in one year in respect of the income, profits and gains of the previous year but, the section provides, this is "subject to the provisions of this Act." Sub-section (1) of Section 59 empowers the Central Board of Revenue to make rules for the purpose of the ascertainment and determination of any class of income; by sub-section (5) the rules made under the section shall have effect as if enacted in the Act; and by sub-section (2) the rules may prescribe the manner in which and the procedure by which the income, profits and gains shall be arrived at in the case of, by clause (ii), insurance companies. The Income-tax Rules, including rule 25 which relates to an Indian life assurance company, and rule 33, which attracts the provisions in rule 25 to a non-resident life assurance company having business in India, were made in pursuance of Section 59; rule 25 is in effect, a provision of the Act and is mandatory in its terms; it provides that the income, profits and gains of Indian life assurance companies, whose profits are ascertained by periodical actuarial valuation, *shall* be the average annual net profits disclosed by the last preceding actuarial valuation. Since Section 3 is subject to the provisions in the Act, of which rule 25 is one, the provisions in the rule prevail over those in the section. When a life assurance company ascertains its profits by actuarial valuation, the amount of the average annual net income, profits and gains disclosed by the valuation is the amount for the purpose of assessment to income-tax, which amount is not obtained by reference to the income, profits and gains of the previous year. Although Section 6 specifies the several heads of income, including interest on Government securities (falling within Section 8), and other sources (falling within Section 12) which are not included in the other heads (covered by Sections 7, 9 and 10) nevertheless the income has not to be assessed separately under the several heads when the total is ascertained by means of rule 25. The ascertainment under the rule of the average annual net profits for the purpose of assessment to income-tax is substituted for the other methods provided by the above sections. In my view assessment cannot be made pursuant to the sections when the rule is applicable.

The next matter for consideration is whether the investments of the Fund and the income derived therefrom form part of its life assurance business. It was argued they do not and that the dividends or interest must be separately assessed under Section 8 and, even assuming that the profits from the life assurance business should be computed according to rule 25, nevertheless the dividends and interest do not come within the ambit of the rule as they do not form part, and are not profits, of that business.

One of the objects of the Fund, contained in clause 3 (d) of the Memorandum of Association, is to invest the moneys of the company, not

immediately required. Insurance business is unlike most other businesses. An insurer receives payments in return for which an obligation arises, dependent upon the nature of the insurance, to pay money upon the happening of the event against which the insurance is effected and which gives rise to payment having to be made. Sudden, unexpected and large claims may be made for which sufficient sources to meet them have to be available, or the premiums in one year may be inadequate to discharge liabilities as and when they crystallize. Investments by an insurance company for those purposes are essential to enable it to carry on its business, to retain the confidence of the public and also its members, particularly in the case of a mutual company, and to be in a position to fulfill its obligations.

Reports of the decisions in the *Liverpool and London and Globe Insurance Company* v. *Bennett* are found, before Hamilton, J., in [1911] 2 K.B. 577, before the Court of Appeal in [1912] 2 K.B. 41, and in the House of Lords in [1913] A.C. 610. That was a case of an English Fire and Life Assurance Company which carried on a fire insurance business in the United States and in the Dominion of Canada, it made investments (called class A) in those countries for the purpose of complying with their laws; and also other investments (called class B) to comply with the laws of New York and other laws of the Dominion; it also made certain voluntary investments (called class C), not under legal obligation, but for the purpose of deriving income from funds consisting of accumulated profits acquired in past years but not distributed among the shareholders and the investments were made in order to have a fund easily realisable, if required. Generally it had not been necessary for the company to realise or expend any part of those moneys for the immediate purpose of carrying on its business as insurers. In each of the three Courts it was held that the investments, including class C, were part of the insurance company's business and the interest derived from those investments was part of the profits or gains of the business. Clause 18 of that company's Memorandum of Association corresponded to clause 3 (d) of the Fund's Memorandum; it provided that one of the objects was to invest moneys not immediately wanted. In respect of Clause 18, Cozens Hardy, M.R., observed, at page 54 of the report in the Court of Appeal, that the object (to invest moneys not immediately wanted) was not a distinct one, the business of the company in all its branches was, in truth, one. In the report in the House of Lords, Lord Parker observed, at page 623, that "obviously moneys invested under this clause (clause 18) are not withdrawn from the business of the company but are retained for the purposes of such businesses, though temporarily invested, so as not to be idle". Elsewhere, at page 623, Lord Parker further observed: "The income and dividends of these investments are, in fact, treated as receipts on account of those businesses and dealt with accordingly, and the capital thereof

is and is intended to be at any time available for the purpose of these businesses. The investments, in fact, constitute a reserve fund, and it is, I think, essential in all such businesses as those carried on by the appellant company that similar reserve funds of this nature should be accumulated". Lord Mersey observed, at page 621: "It is well known that in the course of carrying on an insurance business large sums of money derived from premiums collected and from other sources accumulated in the hands of the insurers and that one of the most important parts of the profits of the business is derived from the temporary investment of these moneys" and later "It is, according to my view, impossible to say that such investments do not form part of this company's insurance business, or that the returns flowing from them do not form part of its profits...........I make no distinction between the three classes of investments (A, B and C)."

The fund carries on the business of life assurance and I see no reason why the principles, regarding such business, laid down in *Bennett's case*, are inapplicable because it is a mutual business. From the decision in that case and the observations by the noble Lords, which I have quoted, it emerges that the investments of the fund form part of its insurance business. The profits from those investments are part of the business profits and those profits, as well as other profits, are ascertained by an actuarial valuation. This was done at the quinquennial valuation as on 31st December, 1934. Incidentally this is an additional circumstance which fulfills the requirements of rule 25 for its application to the fund. *National Mutual Life Association of Australasia* v. *Commissioner of Income-tax, Bombay Presidency and Aden*[1] concerned a non-resident mutual life assurance company which effected 98 per cent. of its total business with members. It was accepted before the Board, in that case, as it was accepted in this reference, that the principles in *Styles' case* applied; the head office of the company was in Melbourne and it had two branches in India; rule 35 of the Income-tax Rules makes the provisions of rule 25 applicable to a non-resident life assurance company, in the absence of more reliable data, to ascertain its income, profits and gains; the application of the rule is also subject, as in the case of Indian companies, to the profits being ascertained by a periodical actuarial valuation; the Australasia company made a return of its Indian business based on one year's account, which the Income-tax Officer did not consider sufficient and he computed the income, profits and gains, under rule 35, upon its last triennial actuarial valuation. Lord Thankerton, in delivering the judgment of the Board, said, at page 112: "There can be no doubt that the total income, profits and gains of the company would fall to be computed on the basis of their triennial valuation reports which, in their Lordships' opinion, is the most reliable method of computation in the case

(1) (1936) 63 I.A. 99; 4 I.T.R. 44.

of a life assurance company. It is the method applied under rule 25 in the case of companies incorporated in India"; later, in the judgment, the assessment was criticised because, assuming, without deciding, that under rule 35 "premium income" should include premiums received from members, it had ignored the principles in *Styles' case*. In my view the Fund's investments and the income derived from them are part of their life insurance business.

Now I come to the matters raised by the third question in the reference, namely, whether the Fund can appropriate its income from investments, its non-mutual receipts, which is mainly received after deduction of tax at source, in the first instance, against expenditure and to charge any balance against the members' subscriptions, its mutual receipts. If this can be done, the whole, or the larger part, of the members' subscriptions will be retained as surplus and will be free of income-tax. In this connection, the Advocate-General confined "expenditure" to "management expenses." He argued that a debtor can discharge his liabilities out of such part of his income or receipts as he may choose for that purpose, irrespective of its source; the expenditure of the Fund is in respect of its business, which expenditure, he contended, can be met out of whatever source of income the Fund may decide to devote to it. He relied for this proposition upon some English decisions and drew particular attention to some observations by Pollock, M.R., in *Commissioners of Inland Revenue* v. *Sterling Trust Ltd.*,[1] and he also cited two decisions by the House of Lords, *London County Council* v. *Attorney-General*[2] and *Edinburgh Life Assurance Co.* v. *Lord Advocate*[3]. I will refer later to those authorities.

Since the profits of the Fund's life assurance business are ascertained by means of a periodical actuarial valuation, rule 25 applies; by this means, the income, profits and gains for purposes of assessment in any year are the average annual net profits disclosed by the last preceding valuation, after making any addition, which the rule specifies, and to which reference is not necessary. All assets and liabilities, including management expenses, are taken into account when computing the valuation and before arriving at the estimated surplus for the period covered by the valuation. In those circumstances the question of an allocation of a special fund or of a particular source of income, out of which the management expenses should be paid, or should be deemed to have been paid, does not arise. Allocation or appropriation with respect to payment of management expenses could only arise if rule 25 were inapplicable and if the income-tax assessment of the Funds' life assurance business were properly made pursuant to other provisions of the Act.

(1) (1925) 12 Tax Cas. 868. (2) [1901] A.C. 26. (3) [1910] A.C. 143

Although, in the light of the opinion previously expressed, allocation or appropriation has really become academic in this reference, since considerable argument was directed to a debtor's right in that respect, I propose to examine the question but this is upon the assumption that rule 25 is inapplicable to a mutual life assurance company.

Mutual dealings arise out of a mutual association. To constitute a mutual association, a number of persons associate together to subscribe money for a fund for the purpose of it being spent upon a particular object, and the balance, if any, being returned to the subscribers and proportionately distributed amongst them. This balance is that part of the fund which is not absorbed by the particular object of the subscriptions. Those transactions are mutual dealings and the unrequired balance is the surplus. This surplus is not assessable to income-tax since it arises out of mutual dealings. It is immaterial whether the association is corporated or incorporated. The contributors are entitled to participate in the surplus, not necessarily immediately, and for the time being it may be held in suspense and may be invested pending distribution. Since the subscriptions are given and received to constitute a fund for a particular object that fund must be used for that object. If other moneys, instead of the fund, are spent upon that object, and the fund is kept intact and not utilised for the purpose for which it is subscribed and obtained, can it be said that the whole fund is the surplus? Can moneys, other than the fund, be used upon the object for which the fund is subscribed so as to create or increase a surplus which would not exist, or not be so large, if the fund had been spent upon the object for which it is subscribed? In my view, not. A surplus from mutual dealings is not the whole of a fund, which is unutilised to pay for the object for which the subscriptions to it are made.

In the present reference the members subscribe to the funds of the General Family Pension Fund. These subscriptions are the mutual dealings with and between the association and its members, which are subscribed for the objects of the association, as set out in its Memorandum of Association. One of the objects is to pay the management expenses out of the funds. Therefore, one object of the subscriptions is to pay those expenses and when received they are readily available for that purpose and should be so utilised. If they are not so spent, they are not used for that purpose. Further, the Fund can, under the Memorandum of Association, invest moneys not immediately required. This must mean that they are to remain invested until needed. The capital of the investments cannot be realised to meet liabilities, *e.g.*, management expenses, when other moneys are available, *e.g.*, members' subscriptions. Since the subscriptions are, I would say, ear-marked for those liabilities to the extent which would be covered by them, if the interest from investments is used to pay for the

management expenses and the subscriptions are not used, that is not dealing with the subscriptions in a correct manner. If other moneys are used to pay for the object for which the subscriptions are received, the whole of those subscriptions is not the surplus after utilisation of the fund for its special purpose.

In the *London County Council* and *Edinburgh cases*, in the House of Lords, there arose the meaning and effect of an English enactment, Section 24 (3) of the Customs and Inland Revenue Act, 1888, which provides that "upon payment of any interest of money or annuities charged with income-tax......and not payable or not wholly payable out of profits or gains brought into charge to such tax, the person by or through whom such interest or annuities shall be paid shall deduct thereout the rate of income-tax in force at the time of such payment, and shall forthwith render an account to the Commissioners of Inland Revenue of the amount so deducted, or of the amount deducted out of so much of the interest or annuities as is not paid out of profits or gains brought into charge, as the case may be; and such amount shall be a debt from such person to Her Majesty, and recoverable as such accordingly........."

The London County Council raised money upon the security of its consolidated loans fund out of which it paid dividends and interest upon its consolidated stock and loans made to it. The Council received (a) rents and profits of lands, (b) interest or annual payments, both being charged with income-tax before receipts, and (c) money raised by rates, not so charged. It paid the dividends and interest upon its loans out of the above three sources of income, and, when doing so, deducted income-tax from the amounts so paid, it retained the income-tax deducted, so far as the dividends and interest were paid out of the rents and profits from land and from interest, upon which income-tax had been charged; but in respect of the payments made out of moneys raised by rates, (which had not been charged with tax), the Council accounted to the Commissioners of Inland Revenue for the amount of income-tax deducted.

The *Edinburgh case* concerned a life assurance company, the business of which included granting annuities. The company's co-partnership contract provided that every policy or other obligation should contain a clause declaring that its capital stock and funds should be the only fund answerable for any demand under such policy or obligation. The company had a large annual income derived from interest, dividends and rents from which income-tax was deducted at source, which was sufficient to pay annuities in full, but this income was not formally appropriated in the books nor was any particular fund specially charged with the payment of the annuities. The company also had an income from premiums. When paying the annuities, the company deducted and retained the amount of tax due in respect thereof

In the above two cases in the House of Lords, payments were made, of interest upon loans by the London County Council and, of annuities by the Edinburgh Insurance Company, out of income from which tax was deducted before it was received by the payers, or debtors. Each debtor had two sources of receipts, charged and uncharged, and sought to allocate the payments to charged receipts and to retain the amount of tax deducted. It was emphasised, by Lord Macnaghten at page 40 and by Lord Davey at page 42 in the *London County Council case*[1] and by Lord Atkinson at page 158 in the *Edinburgh case*[2], that tax is not payable twice on the same income; at pages 42 and 43 in the *London County Council case*, Lord Davey pointed out that the Crown receiving tax on the whole income in the first instance from the owner had no further claim against the mortgagee or annuitant on whose account the owner is deemed to have paid as well as his own and, at page 45, Lord Davey held that the Council was entitled to retain the deductions in respect of income-tax with respect to payments made out of charged income and to account to the Crown only for income-tax on so much of the payments which were made out of uncharged income. The decision in the *Edinburgh case* was to a like effect. It was, in those circumstances, held that the allocations made were correct. In each of those two cases there was no fund out of which payments should have been made and which had not been used for the special purpose nor were payments sought to be deemed to have come from some other fund.

The observations in the *Sterling case*[3], upon which the Advocate-General relies, were made by Pollock, M.R., at pages 879 and 880 where he said that in general principle a debtor has a right to say how the money which he is paying shall be applied and that the party paying has the right to apply the payment as he thinks fit; and, at pages 881 and 882, where a company has two sources of income, charged and uncharged, it is entitled to assume and deem that it has paid according to the most business-like way of appropriating revenue to expenses. That case concerned corporation profits tax imposed by Section 52 of the English Finance Act, 1920; the proviso to sub-section (1) (b) of the section allowed debenture interest to be deducted from the profits of a company before charging to tax. The company had two sources of income, dividends from other companies charged with corporation profits tax before receipt and profits of its business which had not been charged, both of which were paid into one common account. The interest on its debentures was paid out of this mixed fund, which payment the company sought to allocate to the uncharged profits and thus reduce the net income chargeable with tax. The management expenses were also paid out of the mixed fund but this expenditure was not sought to be allocated either to one or to the other of the two sources of income. The company

(1) [1901] A.C. 26. (2) [1910] A.C. 143. (3) (1925) 12 Tax Cas. 868.

was held to be entitled to allocate payment of debenture interest to its uncharged income. In his judgment Atkin, L.J., as he then was, while concurring with the conclusion, said at page 887, that "It is not a question of any rights a creditor has against a debtor, but a question of the right of a person paying the money to pay out of his own funds, and it appears to me that there is nothing in law to prevent a man from paying from any fund,......that is a lawful fund." But, at page 888, the learned Lord Justice added: "If the question of liability, for instance, depended upon whether a man made a payment out of his professional income or out of his invested income, I should have said that that was solved by considering the actual fact whether the money did in fact come out of his professional income or......out of his invested income. If, on the other hand, the question was what were the expenses of his profession, then the fact that he had charged those expenses to invested income or to some other item of income than his professional income would be irrelevant because he could not prevent the fact of it being an expense of his professional income from being determined properly merely by his making a different account in his book." In this case, again, there was not a fund, apart from the mixed fund, out of which the debenture interest should have been paid and there was no attempt to avoid using a fund for its special purpose.

If the General Family Pension Fund allocated the management expenses to interest upon securities, instead of to the members' subscriptions, they would not be using the subscriptions upon the purpose for which they are received and out of which the expenses should be paid; but they would be utilising another fund for that purpose which, in the circumstances, is not a lawful fund, since the subscriptions should first be used, and it would be dealing with the expenses in a wrong manner and somewhat in the same way as the example of improper allocation given by Atkin, L.J. Further such allocation would not be the most business-like way of appropriating revenue to expenses subject to which, it would seem, the Master of the Rolls recognised a debtor's right to allocate.

The last three decisions in England were made with reference to provisions in English Statutes, which do not find a place in the Indian Income-tax Act, permitting deductions in certain instances; in those cases, the taxpayers did not seek to avoid using receipts ear-marked for particular payments, which payments were sought to be allocated to other receipts. I am unable to find that those decisions afford authority for the fund to allocate payment of its management expenses out of its interest income instead of utilising the receipts from members' subscriptions for that purpose.

Lastly, although it is the first question referred, there remains whether an Income-tax Officer is bound to continue to assess a taxpayer upon the same principles followed in previous years. The Advocate-General

abandoned the contention raised in that question, that an alteration in the method of assessment in subsequent years cannot be made by reason of the principle of res judicata. He argued, however, with respect to the second assessment for 1937-38, that since there was one assessment for that year, a second assessment could not be made and the first one discharged, in the absence of any fresh facts. *Sankaralinga Nadar* v. *Commissioner of Income-tax, Madras*[1], and *Commissioners of Inland Revenue* v. *Sneath*[2] were cited during the argument. This is not raised by the first question and I do not consider the Court is required to express an opinion upon it, or in the circumstances, to give an answer to that question.

I would answer the second question in the affirmative and the third question in the negative.

The assessees are entitled to their costs to be taxed.

ORMOND, J.—The questions raised in this case are of importance. It is true that since the assessments now before us the Income-tax Act has been amended by the inclusion of a new schedule governing computation of the income, profits and gains of insurance companies, and that this schedule has been made directly applicable to mutual concerns. Whether or not certain points now raised in this case may possibly arise also directly or indirectly in connection with the application in future cases of the schedule, we are not now adjudicating on the position as it stands today under the schedule but as it stood before the schedule. The nature of the decision to be arrived at in the present case in any event is one that will make a difference to the extent of large sums to the assessee company.

In spite of the directions (at page 1 of the Paper Book) for one reference (meaning presumably the papers for one case relating to one assessment year) to be printed, this has not been done in any clear simple way. The result is that it is not as easy as it should be to trace the details of the various orders made relating to any one of the years of assessment with which the four appeals before us are concerned. The history of the various assessments actually made is found to be this.

As regards the earlier years of assessment between 1928-29 and 1933-34 (inclusive) :—These were originally made on the company not as a life insurance company at all. Then by an order dated 20th July, 1934, the Appellate Assistant Commissioner acting under Section 31 (3) (b) set aside those assessments and directed in effect :—

1. That the assessee company should be treated as a life insurance company.

2. And, accordingly, that it should be assessed under rule 25.

Acting on that decision, the Income-tax Officer then made a revised assessment under rule 25. But in doing so he charged the company to

(1) (1930) 53 Mad. 420. (2) [1932] 2 K.B. 362.

tax on an amount of income, profits and gains represented by the figure of the full ascertained surplus (reduced to an average annual figure) shown I presume by the actuarial valuation for the last period of years for which such a valuation had been made. The figure for this for which he charged the company to tax was I understand Rs. 4,13,397. Thereafter by a supplementary further order dated 28th August, 1937, the Appellate Assistant Commissioner gave directions for such revised assessment of the Income-tax Officer to be modified. He directed in effect :—

3. That the principle of non-liability to tax of the mutual receipts of a mutual society as laid down in *Styles' case* should be applied to these assessments for the years 1928-29 to 1933-34.

4. That the assessee company should be given the benefit of the principle of favourable appropriation as he deduced it from the *Edinburgh case*.

These four points, as I have here noted them, will be seen to be the main points on which all the disputes regarding the various assessments have turned.

The Appellate Assistant Commissioner then states his final decision in relation to these assessment years, 1928-29 to 1934-35, in these words (at page 6) :—

" The excess of expenditure over non-mutual receipts for the quadrennium therefore came to Rs. 2,39,498. From these figures it will be seen that the non-mutual income has been completely absorbed by the expenditure, and in these circumstances it must be held that the entire surplus of Rs. 4,13,397 arose from mutual sources of receipts and is therefore not taxable."

For the purpose of the application by him of rule 25 the Appellate Assistant Commissioner took into account a period of 4 years (it does not appear from the materials before us which 4 years) and worked on figures taken from an account which he refers to as " the Life Fund Account."

The course of reasoning involved in this decision it will be seen must I think be this: Take the actual expenditure (Rs. 19 lacs odd): Pay this first out of the non-mutual actual receipts (Rs. 16 lacs odd) as far as these will go thus absorbing them entirely; then pay the remaining balance of the total of expenditure (say Rs. 3 lacs approximately) out of the mutual receipts (Rs. 7 lacs odd); you thus arrive at a resultant balance or surplus said to consist of the unused portion of the mutual receipts; then, because these mutual receipts are not taxable you conclude that no tax is payable by the company on these assessment years in any respect. (I shall come back to this).

The assessee company was then assessed in accordance with the foregoing decision of the Appellate Assistant Commissioner for the assessment

years 1928-29 to 1934-35. It was also assessed on the same lines for the assessment year 1935-36. Its income for each one of these two assessment years was computed as *nil*. Moreover refunds were directed to be allowed to it on all income-tax already paid by it by deduction at source in respect of interest received on investments.

In pursuance of that decision of the Appellate Assistant Commissioner the assessee company was after that assessed on precisely similar lines and with similar effect in respect of the assessment years 1936-37 and 1937-38. Its income for each of these two years also was again computed as *nil*. And it was allowed refunds for any income-tax already paid by deduction at source. The amount of refund ordered (as shown by the original assessment order for 1937-38 dated 25th January, 1938, handed up by counsel by consent) was, inclusive of income-tax and surcharge, Rs. 69,777-14-0.

It may be noted in passing that this sum included both income-tax and surcharge deducted at source during the accounting calendar year 1936 (Rs. 62,385-10-0 and Rs. 7,283-7-0) and also a sum (Rs. 108-13-0) comprising one fifth on income-tax suffered at source on dividends received in the five year period 1930—1934.

When the time came for assessment for the year of assessment 1938-39, however, the Income-tax Officer (as stated in the statement of case) (para. 6) made a change in the method of assessment. He proceeded to make the assessment directly under Section 8 and Section 12 of the Act on separate calculations for "interest on securities" (under Section 8) and for income, profits and gains under the head "other sources" under Section 12. The receipts charged by him to tax under Section 12 were in fact for the most part interest on securities also; but such being interest on non-Indian securities brought into British India, as were not covered by Section 8. He made no assessment under Section 10 for profits and gains under the head "business" evidently taking the view, since the assessee was a mutual concern, either that it had no business, or that, apart from the receipts already brought to charge under Section 8 and Section 12 it had no further taxable profits, on the ground that whatever might in a non-mutual company have been classed as profits and gains of its business would be for this mutual concern, on the application of *Styles' case*, mere mutual dealings not liable to tax. (A copy of this assessment as made by the Income-tax Officer on 16th January, 1941, is printed at page 7 of the Paper Book). The figures were taken by him not from any actuarial report but from figures of actual receipts and actual expenditure as shown in the assessee's accounts during the accounting year from 1st January to 31st December, 1937.

At the same time as making the new assessment for the year of assessment 1938-39, the Income-tax Officer also served on the assessee a notice

under Section 34 in respect of the year of assessment 1937-38 for the purpose of reopening that assessment. And he made a revised assessment for the year 1937-38 on the same lines as his new assessment for the year 1938-39. The revised assessment for 1937-38 as then made by him is set out at page 9 of the Paper Book. Both these assessments were made on 16th January, 1941 (the date 1943 on page 10 being a misprint).

From these two assessments for 1938-39 and 1937-38 the assessee appealed to the Appellate Assistant Commissioner.

That appeal was disposed of by an order of the Appellate Commissioner on 19th/23rd December, 1941. The effect of his order then made was:—

1. That these two assessments of the Income-tax Officer should be set aside.

2. Revised assessments for each of these two years should be made applying rule 25.

3. But at the same time, as stated in the statement of case, he also directed that "interest on securities" should be separately assessed under Section 8 (allowing as deduction against these only bank commission as mentioned in Section 8). Also that income, profits and gains from "other sources" should also be separately assessed under Section 12, bringing in interest on non-Indian investment brought into India which would not be within Section 8, (allowing a deduction against this head for proportionate expenses of management). A copy of his order is printed at page 15 of the Paper Book.

From this order in respect of both the years of assessment (1937-38 and 1938-39) both parties (the assessee and the Income-tax Officer) appealed to the Appellate Tribunal.

These appeals were disposed of by four different orders of the Appellate Tribunal, being orders in R.A.A. Nos. 76 and 77 and orders in R.A.A. Nos. 83 and 84.

In the R.A.A. Nos. 76 and 77 the two appeals by the Income-tax Officer in respect of the assessments for 1937-38 and 1938-39 were allowed and the Appellate Tribunal directed in effect:—

1. That the order by the Appellate Assistant Commissioner for assessment under rule 25 was wrong.

2. Beyond this the Tribunal merely directed that the Income-tax Officer should re-compute the income "in accordance with law." (The orders dated 28th July, 1942, are printed at page 23 of the Paper Book).

Appeal R.A.A. No. 83 related to the objection raised by the appellant assessee in respect of the assessment for 1937-38 in which the assessee (besides other objections as in the assessment 1938-39) took the objection that the Income-tax Officer was not justified in reopening the assessment

under Section 34. The Appellate Tribunal held the Income-tax Officer was justified. (Their order dated 28th July, 1942, is printed at page 24 of the Paper Book).

Appeal R.A.A. No. 84 was an appeal by the assessee company in respect of the assessment year 1938-39 against the order mentioned above of the Appellate Assistant Commissioner dated 19th or 23rd December, 1941. Briefly the contentions of the assessee company raised in this appeal were :—

1. That the coupling of the direction of the Appellate Assistant Commissioner to make the assessment in accordance with rule 25 with another direction to make the assessment of interest on investments under Section 8 and of income, profits and gains from other sources under Section 12 was illogical and illegal.

2. That the company maintained the Appellate Assistant Commissioner was right in directing assessment under rule 25.

3. That the assessee was entitled to the benefit of favourable appropriation as laid down in the *Edinburgh case*; that in pursuance of that principle it should be held that the company had met its expenses first from its non-mutual receipts, absorbing all these, so that any surplus of receipts must be derived from mutual dealings; and that the result should be held to be, as contended by the assessee, that there was finally no taxable income for assessment. (The order dated 28th July, 1942, is printed at page 25 of the Paper Book).

It was ordered that the Appellate Assistant Commissioner's direction that the assessment should be made under rule 25 was not correct.

To this extent his order was modified. But except in this respect (which was in fact on a point not taken by the assessee, who wished to have the assessment made under rule 25) the directions given by the Appellate Assistant Commissioner were upheld and the appeal of the assessee was dismissed.

The ever-changing seesaw effect of these various decisions in these long drawn-out proceedings is noteworthy. The first assessment for 1938-39 was originally made only on 16th January, 1941. The decision of the Appellate Tribunal was not reached until 28th July, 1942. The matter now comes before us in February, 1946; nearly 7 years after the end of the year of assessment and more than 5 years after the original assessment for 1938-39 was in fact made.

Though there is an absence of direct language on certain of these points in the order of the Appellate Tribunal the order may, it seems, be taken to mean

1. That the assessee is to be treated as a life insurance company.
2. That rule 25 is not applicable,

3. That the principle of non-liability of mutual receipts on the authority of *Styles' case* is applicable.

4. That the assessment should be made separately of interest on investments under Section 8 and of income, profits and gains from other sources under Section 12.

5. That the principle of favourable appropriation as laid down in the *Edinburgh case* is not applicable.

Thereafter two applications were made under Section 66 (1) of the Act for the statement of a case by the Appellate Tribunal to this High Court against the decisions of the Tribunal in R. A. A. No. 83 and No. 84: (see pages 30 and 32 of the Paper Book).

As a result of those applications the Appellate Tribunal on 15th August, 1943, stated a case (page 1 of the Paper Book) in which the following three questions of law were referred by it for the opinion of this High Court.

1. Whether the decisions of the Assistant Commissioner of Income-tax, Calcutta, for the years 1928-29 to 1935-36 are binding upon the Income-tax Officer upon the principles of res judicata or otherwise.

2. Whether the income, profits and gains of the General Family Pension Fund for the year ending 31st December, 1936, should be assessed under rule 25 of the Indian Income-tax Rules in the form then in force.

3. If the answer to (2) is in the affirmative, whether in applying the said rule 25, from the surplus so ascertained the Fund is at liberty to appropriate its non-mutual receipts, that is income from its investments, in the first instance, against its expenditure and to charge any balance of expenditure against its mutual receipts, that is income from members' subscriptions, thus leaving a final balance of mutual receipts which are non-taxable under the authority of *Styles' case.*

I would first make certain general observations concerning rule 25:—

For an insurance business the actual receipts and actual expenditure in any given year of account give little real indication of the financial state of progress of the business or whether it is heading in the long run towards a profit or a loss. When it is considered that an assured may pay a single lump sum entitling him to receive an annuity payment every year for the rest of his life, it is no proper indication of the solvency or profit of the business to point in one given year to the single large receipt for premium counterbalanced during that accounting year by no outgoing payment at all (which will have to be paid if it all many years later), or to point in another given year to the single small payment for an annuity for that year counterbalanced during that accounting year by no incoming receipt at all (since the premium will have been received many years before). So with all other dealings in connection with life insurance other than actual annuities.

Such reasons, no doubt, prompted the observations of the Board by Lord Thankerton in *National Mutual Life Association of Australasia Ltd. v. Commissioner of Income-tax, Bombay* [1], when he said (in considering rule 35 in respect of Indian branches of non-resident insurance companies):—

"There can be no doubt that the total income, profits or gains of the company would fall to be computed on the basis of their triennial valuation reports, which in their Lordships' opinion, is the most reliable method of computation in the case of a life insurance company. It is the method applied under rule 25 in the case of companies incorporated in India."

In order to ascertain their progressive financial position it is the common practice of insurance companies to have actuarial valuation reports made on the business of the company at regular periods, commonly at intervals of five years, four years or three years. It is on these reports also that the scale of their charges for premiums for particular classes of business and the amount of bonus decided to be paid out is worked out and reviewed. The assessee company followed this practice, the actuarial valuation reports in its case being for quinquennial periods. During the year of assessment 1938-39 the last existing actuarial valuation report was that which had been made for the five years ending on 31st December, 1934.

An assessment for 1938-39 under rule 25 thus, though it is a computation of the income, profits and gains of the assessee company for that year for assessment purposes of income-tax, is nevertheless based on figures derived from the actuarial report over the five years 1929-34; from which is in fact calculated, by taking one fifth of a total figure, a figure representing an annual average figure.

One feature of rule 25 is that it contemplates a computation of a radically different nature and founded on a radically different basis to that normally adopted for computation of income under Section 8 or Section 10 or Section 12.

Computation of income whether of interest on investments under Section 8 or of profits and gains of a business under Section 10 or of income, profits and gains from other sources under Section 12 is in every case based on actual receipts or on a surplus of actual receipts over actual expenditure during a particular year of account. This is not so for the computation made under rule 25. Here the computation is based on a comparison between the latest actuarial valuation report and last made previous actuarial valuation report of five years before.

For the purposes of the actuarial valuation report the prospective liabilities and prospective assets of the company are taken at a valuation on a capitalised or discounted basis to represent their valuation at the date

(1) (1936) 63 I.A. 99, at p. 112; 4 I.T.R. 44, at p. 54.

of the report, after allowing for the prospects of the length of life of the assured on actuarial life tables. Assuming the company is in a solvent state, a surplus will be shown of the valuation of assets on that date over the valuation of liabilities. A difference can then be struck between the figure for surplus on the current actuarial valuation report and the figure for surplus on the last preceding actuarial valuation report made five years before. Such difference is (subject to minor adjustments) taken for the purposes of income-tax as the total income, profits and gains of the company over the five year period covered by the current actuarial valuation report. And one fifth of this is then taken as the average annual income, profits and gains for that period.

While one particular actuarial valuation report may show as a "surplus", a figure representing a difference as on that date between the valuation of potential assets over the valuation of potential liabilities, this is not any measure of the income of the assessee for purposes of tax. It is the excess of this surplus shown in the current actuarial valuation report over the surplus shown in the last made previous actuarial valuation report, which has to be taken as the income for the five years covered by the current report for the purposes of income-tax. This is referred to in the observations of Lord Thankerton in the case of *National Mutual Life Association of Australasia Ltd.* v. *Income-tax Commissioner, Bombay*[1], when he remarked :—

"A single valuation report as at the end of the year of account would obviously not have been sufficient for the ascertainment of profits; it would be necessary to have a valuation as at the *terminus a quo*..."

It will be seen that the difference (in an upward direction) between the two different figures for surplus at the beginning and at the end of the five year period may depend on elements wholly independent of actual receipts. As an illustration: supposing there are on the books of the company 20 persons of varying ages between 45 and 55, who, having paid up in full all premiums on their policies, are entitled to receive from the company payments of annuities of varying sums for the rest of their lives, a certain figure is taken as the valuation of the liability of the company on their policies. When the actuarial valuation report for 1929 is made, a figure is taken into account on the debit side representing a single capitalised or discounted liability as at a valuation at the date of that report of all future annual prospective liabilities relative to those assured persons over the period (on life tables) of their expected lives; which may be for varying periods in some cases up to as much as another 20 years or more. This figure is an element (on the debit side) in the calculation of the surplus of assets over liabilities on the date of the actuarial valuation report of 1929,

(1) (1936) 63 I A. 99, at p. 111; 4 I.T.R. 44, at p. 53.

Then suppose all those 20 persons die prematurely in 1930. When it comes to make the actuarial valuation report of 1934 the debit figure for liability of the company in respect of the policies of those 20 persons (now deceased) will have vanished to zero. The difference in the surplus of 1934 from the surplus of 1929 will have been increased (among other elements) by the elimination of that debit figure. By that amount (irrespective of other elements) the profits of the insurance company (if a non-mutual company) will have been increased by the difference between that debit figure as it stood in 1929 and as it now stands at zero, in 1934. Yet there will have been no actual receipts during the 5 year period covered by the report which can be said to be responsible for this profit.

In the actuarial valuation report in addition to taking account of the valuation of prospective assets and liabilities arising from premiums expected to be received and payments expected to be made on policies, account is also taken on the valuation of the assets of the company arising from its investments as the position is assessed on the date of the report. In addition to receipts or prospective receipts for interest, capital appreciation or depreciation may thus come to be reflected in the report, such as would not be included in an assessment of interest on investments if made under Section 8. If it is correct to hold, as I do hereafter, that for an insurance company such as the assessee company it is an integral part of its business to manage its investments such a result of inclusion as "profits," for the purpose of taxation, of surplus derived from an appreciation in capital value of investments, may very possibly, as it seems to me, come to be held to be not incorrect or anomalous. Should it be found necessary to exclude this element from the final notional figure on which tax is to be charged, no doubt the final figure could be adjusted. I am not here concerned with that aspect of the matter. I only refer to this as showing another feature of difference between a computation under rule 25 and a computation under Section 8 (with Section 10 or 12).

It is clear therefore that the computation of income, profits and gains under rule 25 is of a nature very different to the ordinary computation for purposes of Section 8 or Section 10 or Section 12 based on actual receipts and actual expenditure in a particular year. It was having regard to such considerations as these, that for convenience in the course of the hearing we referred to the figure representing the difference between the two surpluses as a "notional figure" representing income. When one-fifth of that figure representing notional income for 5 years is taken, this also is a "notional" figure for one year's income, profits and gains. It is this notional figure under rule 25 on which tax is then to be charged. It is convenient to refer to it as a "notional" figure for purposes of distinction from figures relating to actual receipts or actual expenditure.

Another feature of rule 25 is that it contemplates an accounting period radically different from that normal under Section 8, 10 or 12. For assessment under Section 8, 10 or 12 the year of account is taken as the year previous to the year of assessment as is the effect of the following provision of Section 3 :—

" tax............shall be charged for that year (*i.e.*, year of assessment) ....in respect of all income, profits and gains of the previous year......"

By Section 13 it is also provided that " income, profits and gains shall be computed for the purposes of Sections 10, 11 and 12 in accordance with the method of accounting regularly employed by the assessee."

The assessee company kept its accounts by calendar years. So for the year of assessment 1st April, 1937, to 31st March, 1938, if assessed under Section 8 the income computed would be actual receipts of interest actually received during the accounting year between 1st January and 31st December, 1936. But for application of rule 25, the position would be different. In 1937 the last quinquennial actuarial valuation report to have been made would be the one for the five years ending on 31st December, 1934. So the computation under rule 25 of income, profits and gains would be based on a difference in the surplus (of potential assets over potential liabilities) at 31st December, 1934, from the surplus at 31st December, 1929; for which the company's actual transactions over these 5 years and of nothing later than 31st December, 1934, would form the basis of calculation. It is clear that none of the actual receipts actually received and none of the actual expenditure actually spent during the accounting year 1st January, 1935, to 31st December, 1936, could find any place or reflection in the actuarial report for the quinquennium ending 31st December, 1934. Moreover for assessments made under rule 25 the same notional figure for average annual income, profits and gains would be worked on for a consecutive period of five assessment years until the next actuarial valuation report came out. Since it is only five earlier accounting years (*e.g.*, 1929-1934 for an actuarial valuation report of 31st December, 1934, for the assessment year 1937-38) which can be reflected in the actuarial valuation report, it comes to this; for any computation made under rule 25 an average of a notional figure based on five earlier accounting years is taken as the basis of assessment instead of an actual figure for one year based on a single accounting year immediately preceding the year of assessment.

In view of what has been said it naturally follows, I think, that a computation under rule 25 is not compatible with and cannot be combined with any computation under Section 8 or 10 or 12. This also I think follows from the language of the rule itself. Its wording is :—

"...*the income, profits and gains* of the Life Assurance *Business* shall be the average annual net profits disclosed by the last preceding valuation...."

Now the "profits and gains" of the "business" are what are normally, apart from the rule, assessed under Section 10; the "income, profits and gains" from "other sources" are what are normally assessed under Section 12, and the "interest on securities" is what is normally assessed under Section 8. Since interest on securities is certainly "income", all the three classes of receipts referred to in Sections 8, 10 and 12 come within the all-embracing expression "income, profits and gains" of rule 25. The only question is whether by describing these in rule 25 as "of the Life Assurance *Business*" it is intended therefore to exclude interest on securities or income, profits and agains from other sources. In the view I take, as later explained, that the management of its investments is, in the case of a life insurance company, an integral part of the business, it follows, I think, that in a case where rule 25 is applied, the computation of income from interest on securities is intended to be included in the computation made under rule 25 and based on the actuarial valuation report; and that no separate assessment under Section 8 of interest on securities is contemplated. Interest on investments of non Indian companies (such as sterling companies) brought into India which, apart from the rule, might be assessed under Section 12 are also similarly intended, I think, when a computation is to be made under the rule to be brought into the same calculation based on the actuarial valuation report as being "income, profits and gains" of the company's "business".

I need not here consider whether there might be any receipt other than interest on investments which as outside the business might be open to separate assessment under Section 12. There are no such other receipts concerned so far as I am aware in the present case. Apart from considerations arising on the wording of the rule, it would, I think, also be highly impracticable in any practical working of the rule when rule 25 is applied, and a computation is made under it based on the actuarial valuation report, to make any separate assessment under Section 12 in respect of interest on investments. As already observed the investments are taken into account for the valuation in the actuarial valuation report. Not only would there be the ordinary intricacies of calculation in arriving at a figure for their exclusion from the difference in the two surpluses taken at the two dates at five years intervals, but there would be the added difficulty that, while investments and interest therefrom as reviewed over a specific 5 years say between 1929 and 1934, would be being taken into account for the actuarial valuation report, investments (probably different) and interest therefrom during a different period (a later accounting year say of 1936) would be being taken into account for any assessment under Section 12.

It is clear therefore that the basis of computation for rule 25 is radically different from that under Section 8 or Section 10 or Section 12; that

the relative accounting period for an assessment made under rule 25 is radically different from the accounting period for Section 8, 10 or 12; also in my view that it is not contemplated under the Act that there should be any separate assessment of interest on securities under Section 8 conjointly with an assessment of income, profits and gains of the insurance business under rule 25. In my view either rule 25 applies to this case; in that event the assessment is to be made under rule 25 without reference to Section 8, 10 or 12; or it does not; in that event the assessment is to be made under the appropriate provisions of Section 8 and/or 10 and/or 12 without reference to rule 25.

With these general remarks which will I believe enable me to shorten what I have to say later, I will now pass to consider the next point, whether rule 25 is applicable in the case of this mutual insurance company or not.

The main arguments advanced by Dr. Gupta on behalf of the Commissioner of Income-tax as objections to the applicability of rule 25 to this case, if I may summarise them, were in effect: (i) That the assessee company not being a life insurance company for the purpose of the Life Assurance Companies Act of 1912, by reason of its having been expressly exempted from the provisions of that Act by Government Notification, it was not a life insurance company under the contemplation of rule 25; (ii) That the assessee company had no business; since what would have been insurance business in the case of a non-mutual company was in the present case of a mutual concern mere mutual dealings. Having no business, it accordingly had no profits. Alternatively even if it be correct to say that the assessee company carried on insurance business, yet it was precluded by its own articles and memorandum of association from making any income, profits or gains from its business. In respect of its mutual receipts, by the rule in *Styles' case* being a mutual concern it could not have profits. And in respect of its interest on investments these were not included in the term "business" mentioned in rule 25; since the management of its investments did not form an integral part of the company's "business". In any event, having no profits, the assessee company was therefore outside the rule. (iii) That, conceding, as he did, that the principle of *Styles' case* was applicable in India, any application of rule 25 did not make sense; and the rule became impossible of practical application and could not be worked out.

Regarding the first of these objections: In my view rule 25 is not restricted to insurance companies governed by the Act of 1912 for reasons already stated by my learned brother. Had this been intended it would have been easy to say so. In my view the rule applies to all insurance companies. The assessee company carries on in my view insurance

business and it is a company incorporated under the Indian Companies Act, therefore it is an insurance company within the meaning of rule 25.

I pass now to the second of these objections.

Regarding the question whether the assessee company being a mutual concern carries on business, that there had at one time been some degree of controversy on this point is seen from the change of view expressed by Brett, L.J., in his own two judgments; first in inclination of the view in *Smith* v. *Anderson*[1] and later in *In re Padstow Total Loss and Collision Assurance Association*[2]. Any such controversy has however been set at rest. For authority that it is now well settled that a mutual insurance company in respect of its mutual dealings does carry on business, it is enough for me to refer only to the decision in the House of Lords in *Commissioners of Inland Revenue* v. *Cornish Mutual Assurance Co., Ltd.*[3] Indeed it was in the course of the hearing conceded by Dr. Gupta that the assessee company did carry on business.

Regarding the question whether the assessee company makes profits within the meaning of rule 25, if I may deal with this under the heads of the following 4 different points, the position becomes as I see it clear.

Firstly, it appears to me a correct contention speaking for myself that the profits (or the income, profits and gains) referred to in rule 25 mean taxable profits.

Section 3 makes income-tax chargeable under the Act in respect of all income, profits and gains. Section 4 provides that save as hereinafter provided the Act shall apply to all income, profits and gains as described or comprised in Section 6 (derived etc. in British India). Section 6 relates to the various heads of income, profits and gains which are chargeable to tax. It follows directly from Section 3 as well as on the general tenor of Sections 4 and 6 and of the Act as a whole, in my view that with the exception of cases concerning particular express exemptions the word "profits" and the word "income" when read in the Act must be taken to mean taxable profits and taxable income.

Therefore I do not feel it open to me to say that the word "profits" in rule 25 can be taken in the first instance, when testing whether the rule is applicable or not, to mean profits not liable to tax.

For this reason I do not feel, when applying the rule to a mutual company, to ascertain its income, profits and gains, that you would be justified in making a computation in which you took account of all matters (including in this case mutual dealings) which you would take into account if the company were a non-mutual company. In my view the computation to be made under the rule can only mean a computation of the income,

(1) [1880] 15 Ch. D. 247, at p. 280.
(2) [1882] 20 Ch. D. 137, at p. 148.
(3) (1926) 12 Tax Cas. 841.

profits and gains liable to tax. I agree with Dr. Gupta's argument therefore this far that the rule then will only be applicable to a company which has or may have profits in this sense of "profits chargeable to income-tax."

Secondly, on the authority of *Styles' case* which, it was conceded by counsel on both sides, is applicable in India, any surplus resulting from mutual dealings in the insurance business of a mutual concern such as the assessee company does not constitute a profit chargeable to income-tax.

Thirdly, it may now be taken, I think, as settled, in view of the decision in the case of *Liverpool and London and Globe Insurance Company* v. *Bennett* [1913] A.C. 610 (in the House of Lords) (reported also in [1911] 2 K.B. 577, and [1912] 2 K.B. 41, as to the hearing in the Court of first instance and on appeal) that the management of its investments is an integral part of the business of an insurance company. If this is so in the case of an ordinary non-mutual insurance company, it must, it seems to me, be equally so in the case of a mutual concern such as the assessee company in the present case.

Fourthly, in the present case it is not suggested that the interest on investments is not income or profits which are liable to tax. This interest is clearly not derived from mutual internal dealings among the members but from dealings with persons outside. The Advocate-General indeed conceded that interest on its investments would be liable to tax. Since the investments are in the case of this insurance company part of its business, it follows that profits from its business do exist.

Since it employs actuarial reports, and is an insurance company, and has business, of which there are or may be profits, in my view rule 25 directly applies in terms on its clear wording.

Since it applies, the computation for assessment should be made under rule 25 and not under Section 8 or Section 12 or Section 10. I may here mention that Dr. Gupta also contended, even if rule 25 was held at all to be applicable to the assessee company, then :

1. That rule 25 does not provide the only method of computation of the income, profits and gains of the companies with which it deals. That Sections 8, 10 and 12 of the Act are neither abrogated nor excluded by rule 25. Therefore assessment separately under these sections is open to the Income-tax authorities as an alternative method to rule 25. And :

2. That application of rule 25 (if at all applicable) was limited to the life assurance business; that this did not include interest on investments; and that assessment for this should be made separately (independently of the assessment if any of the assurance business under rule 25) under Section 8 and Section 12.

The effect if these contentions were accepted would be to justify in their entirety the assessments made by the Appellate Tribunal. For, since

the insurance business was mutual, there would be nothing to assess; and if the interest on investments were assessed under Sections 8 and 12, there would be no room for any available deductions beyond those allowed by the Income-tax Officer in those assessments as made by him.

In view of what I have already said earlier in this judgment, it is unnecessary for me now to say more as to these contentions concerning an alternative or partial application of rule 25. Holding as I do that for this insurance company the management of its investments is an integral part of its business, and in view of the obligatory wording of rule 25 (by use of the word "shall") and holding as I do that rule 25 is applicable to this case, there is no room in my opinion for any assessment under Section 8 or Section 12 in this case.

The position then is, since the management of its investments forms an integral part of its business, this assessee company has a combined business which includes its mutual insurance business and the management of its investments. On this position rule 25 has to be applied in a manner to achieve computation of profits from that side of the combined business which deals with and produces the profits from investments; but not from that side of the combined business which is concerned with the mutual dealings in insurance.

The real difficulty to my mind arises as to the method of application of rule 25. This is the substance of the third of the objections as I have stated them above. By what method of calculation are the profits and gains of the business to be arrived at so as to exclude from the computation any receipts which in the case of a non mutual insurance company would be profits but in the case of this mutual concern are not profits and so as to find the taxable profits for the purposes of assessment under rule 25; that is to say "the average annual net profits from the actuarial valuation" and as "disclosed by the last preceding valuation." I agree with Dr. Gupta that the matter presents practical difficulties.

By the question of law referred to this Court we are not asked however to express any opinion as to how this calculation is to be made in detail. Nor are we asked how rule 25 is to be applied in general, but whether it is to be applied. We are however asked one particular question in connection with the method of application of rule 25; that is in effect in question 3, if the rule is to be applied, whether, as contended for by it, the assessee company is entitled to invoke and take advantage of the principle laid down in the *Edinburgh case* to which, for brevity, I shall refer as the principle of "favourable attribution."

In support of the principle of favourable attribution the learned Advocate-General relied principally on four reported cases, being *London County*

Council v. *Attorney-General*[1]; *Edinburgh Life Assurance Company* v. *Lord Advocate*[2]; *Sterling Trust Ltd.* v. *Commissioners of Inland Revenue*[3] and *Fenton's Trustee* v. *Inland Revenue Commissioners*[4]. The general principle for which those cases were cited as authority was, as compactly stated in the judgment of Pollock, M.R., in the *Sterling Trust case*[3], as follows:—

"......that where you are considering the business of a company which has two sources of income, the one subjected to tax and the other not, you are entitled to assume and deem that it has paid the money that it ought to pay according to the most business-like way of appropriating the revenue to the expenses; further, that even though that has not been done in fact by any separate allocation of the money, as was done here (that is, in the *Sterling Trust case*) in the later years by putting it at a special bank, still you are entitled to treat the money as having been paid out of the fund which is most favourable to the company, which is, in this case, the tax-payer."

The same principle was in the *Sterling Trust case* held to be equally applicable whether the assessee was seeking to show "as the most favourable method of payment for himself" payment out of the taxed income or payment out of the untaxed income. In the *Edinburgh case* and other cases the assessee was contending that moneys had been paid out of funds already charged or subject to charge. In the *Sterling Trust case* it was the other way about. That this made no difference is clear from the passage in the judgment in the *Sterling Trust case* of Atkin, L. J., at page 887 when he said: "So far that seems to me to establish what was undoubtedly in all those cases a material fact, namely, that the annuities or the interest whatever it might be, was paid, and paid out of, in that case, the taxed income; and I think the same principle leads one to the conclusion that in this case where the advantage is the other way to the tax-payer, that the payment of the debenture interest was paid out of the untaxed income."

In the *London County Council case* the point arose in relation to Section 24 (3) of the Customs and Inland Revenue Act, 1888, because under that section in paying the dividends on their consolidated stock out of the Consolidated Loans Fund the London County Council were bound to account to the Crown for the income-tax which they deducted from the dividends "*so far only as the dividends are not paid out of their income which has already been charged with income-tax.*" The question was therefore whether the dividends they were paying to their shareholders were being paid out of a fund which had already been charged with income-tax or out of a fund which had not been so charged.

(1) [1901] A.C. 26.
(2) [1910] A.C. 143.
(3) (1925) 12 Tax Cas. 868.
(4) [1936] 2 K.B. 59.

In the *Edinburgh case* the question was again a similar question arising in the same way on Section 24 (3) of the Customs and Inland Revenue Act of 1888. There it was again a question whether the interest or annuities being paid by the company "had been paid out of profits or gains brought into charge." In the *Sterling Trust case* the question arose in relation to Section 52 (1) (b) of the Finance Act, 1920. The terms of the section are set out at page 871 of the report of that case. Under that section tax was only payable "after deducting from the amount of profits any interest or dividends *actually paid out of those profits*." Section 53 of the Finance Act, 1920 (see page 876), being the section showing how the profits are to be assessed on which the tax shall fall, contains an express proviso that there should not be included in the profits subject to the tax (*i.e.*, the Corporation Profits Tax) "the interest, dividends, or income received directly or indirectly from a company which was liable itself to be assessed to Corporation Profits Tax in respect thereof." So the question in the *Sterling Trust case* also was a question similar to that in the other two cases, that is, whether the debenture interest paid to the debenture-holders by the company had been paid out of a fund consisting of dividends received from companies already charged (or liable to be charged) to Corporation Profits Tax or out of some other fund which in the hands of the company would be admittedly liable to Corporation Profits Tax.

The question then is: is that principle of favourable attribution as laid down in the *Edinburgh case* and those other cases to which I have referred, to be applied in the present case? In my view it should not for the following two reasons; firstly, because the main problem here is quite different; secondly, even if the main problem were the same, because the necessity for the assessment in the present case being made under rule 25 entails an assessment on a basis of valuation, which is not dependent on or directly concerned with actual payment, and therefore no question of attribution of payments arises at all. It stands to reason that any principle of attribution entails a notion of attribution of some payment to any particular fund, as having been made from, or as having been deemed to have been made from, that particular fund. And if there are no actual payments to be considered, there can be no process of attribution. I should, to explain myself better, enlarge slightly on these two reasons.

In the first place the question arising in the present case is entirely different to my mind from that which arose in those cases to which the principle of favourable attribution was held to be applicable. There the question was whether or not moneys were being paid by the company to persons entitled to receive payment from the company from a fund of a particular class or from a fund of another class; the question was whether the moneys had in fact been so paid, or whether they should have been

deemed to have been so paid. There was no question arising about calculating an amount of profits. Here the question is, what is the amount of the profit made by the assessee? This entails the question what is the amount of expenses that have been incurred in order to make that profit?

In this particular case it is true a particular difficulty arises since the total surplus of receipts over expenditure of the assessee is earned from a combined business, part of the operations of which are not liable to income-tax and part of the operations of which are liable to income-tax. Were it not for the complication arising from the combined source of earnings the question would be a simple one; what are the total receipts and what are the total expenses that have been incurred in earning the surplus of receipts over expenses? Nevertheless, the question remains no more than this; what is the amount of the profit made? For this computation required to be made under rule 25 the assets and liabilities have to be balanced up *before* any figure for taxable profit is arrived at. There is no taxable profit in existence until the balancing process has been completed. In putting the debits against the credits in order to ascertain the profit, and before its ascertainment, there is no question of making a deduction from a profit that has been ascertained or making a payment out of it in the course of its disposal. The assessee cannot therefore here say: "I am making a payment (of management expenses or of payments on policies) *out of my taxable profits*: or out of a particular fund rather than out of my mutually owned monies received."

Suppose a company had two branches in two different cities under two different persons as managers yet there were dealings common to both branches, and each manager was entitled to commission on the profits of his branch: it surely would not meet the case if the head office told one manager: "the profits of your branch are nil this year because all the expenses both of your branch and of the other branch have in fact been paid out of the receipts of your branch." This simple illustration, though not exactly on all fours with the present case, illustrates what I find it otherwise difficult to put sufficiently forcibly into simple clear words: that (as I see it), attribution of payment has in truth nothing to do with any process for the ascertainment of profit, which must be worked out, and the working out of which must be finished, *before* the profit has been ascertained. This, it seems to me, was what Lord Atkin was referring to when he said (in the *Sterling Trust Ltd.* v. *Commissioners of Inland Revenue*[1]) when giving an illustration :—

"If, on the other hand, the question was what were the expenses of his profession, then the fact that he had charged those expenses to invested income or to some other item of income than his professional income

(1) (1925) 12 Tax Cas. 868, at p. 888.

would be irrelevant because he could not prevent the fact of it being an expense of his professional income from being determined properly merely by his making a different account in his book, and I do not think the cases go to any different decision than that."

What is I think a related aspect of the matter was also referred to by Lord Halsbury in the *Gresham Life Assurance Society* v. *Styles*[1], when he observed :—

"When once an individual or a company has in that proper sense ascertained what are the profits of his business or his trade, the destination of those profits...........is perfectly immaterial."

The present computation to arrive at a figure for profits (though working here under rule 25 on the basis of the actuarial valuation) is similar, I think, to the problem in the illustration taken by Lord Atkin. Inherent in any question "What are the profits?" is the question put by him "What are the expenses?" For profits ,will be calculated by arriving at a balance of receipts over expenses (or in the present case working on the actuarial report a valuation of assets over liabilities). In either case whether in Lord Atkin's illustration or the present case it will to my mind matter not the slightest how or from what fund the expenses may have been met or the liabilities have been or will be met. The only relevant question is what are the expenses (or liabilities when working as here on the actuarial report) proper to be taken into account.

In the *Edinburgh* and similar cases on which the assessee relies it was a question of following monies to see whether they were monies on which tax had already been paid because if so they were exempt from paying tax again. Here there is no question of following monies to identify them.

In the second place, I would again here emphasize, what I already referred to in my introductory remarks concerning rule 25, that in a computation made under rule 25 no question either of actual receipts or of actual expenditure arises. The matter rests on a footing of assets or potential assets and of liabilities or potential liabilities as reduced to a static valuation figure as on the date of the actuarial valuation report. So there is no question either of actual expenses of management or of actual payments on policies being deducted from any figure in order to arrive at the profits under rule 25. The essence of the principle laid down in the *Edinburgh case* is that what is there being considered are actual payments and actual receipts; the question being whether a particular payment made could be said to be "attributed to"—in the sense of being paid out of—a particular fund consisting of actual receipts. In this computation now to be made under rule 25, no actual expenditure and no actual receipts are contemplated; since the whole matter rests on a surplus of assets over

(1) [1892] A. C. 309, at p. 315.

liabilities on mere valuation figures (taking into account prospective future liabilities and future assets) and on a difference between a surplus at the terminus at the end of a five year period from a surplus at the *terminus a quo* at the beginning of the five year period. The surplus itself is only notional figure. Since there is no question of actual expenditure or actual receipts there can be no question of attributing payment in fact to any particular class of receipts or to any particular fund.

The result is, I hold therefore, that the principle of favourable attribution as exemplified in the *Edinburgh case* for example, is not applicable to the present case.

This brings me back again to the third objection raised by Dr. Gupta concerning the actual application of rule 25 as a practical proposition in the present case. Is there any difficulty making it so impracticable in application as was suggested by Dr. Gupta as to make it proper for us to hold in spite of its terms, that on a general construction of the Act it is impossible for the legislature to have intended that rule 25 should be applied in such a case as the present?

There is another aspect of this matter in so far as practicability of application is concerned. Some comment was made in argument, and I think justifiably, in regard to certain of the rulings given in this case by one or other of the Income-tax authorities, that whether or not the ruling was legally or theoretically when analysed correct, yet, it was expressed in terms which made it very difficult for the Income-tax Officer when doing the practical work of assessment to know how he was to act. In view of the length of time over which the doubts and disputes over these assessments have been running on, it will be of benefit to the parties, I think, if when giving my ruling in this appeal I give as clear an indication as possible of a course which the Income-tax Officer may adopt when he has to deal with the matter.

Having, on what has been said above, reached the conclusion that there is a combined business, part of the undertaking of which earns profits, liable to income-tax and part not, and that the assessment has to be made under rule 25, the problem is to separate the two parts, or the earnings of the two parts of the combined business.

Two possible approaches might be adopted. Either a figure is taken from the actuarial report (one fifth of the total difference in surpluses over the five years) representing the annual total receipts or (broadly speaking) income of the company, and a proportionate fraction of this is taken as being that portion of it which represents the profits from the taxable side of the business: that is to say the investments. (This would be allowing in effect the benefit of deduction for a proportion of expenses of management against the interest from the investments since the total

expenses of management for the whole business would have been allowed for as liabilities in the actuarial valuation). Or individual figures might be taken from the actuarial report, or from the detailed calculation on which it is based, showing separate individual assets derivable from investments only (excluding assets derivable from mutual insurance dealings) and from these there might be debited some proportional fraction of the total liability figures representing expenses of management. In either case a system of proportion is involved in the calculation.

This brings me to what I reckon to be the last point for determination in this case. Is the use of any such system of proportion in the present case prohibited or legally unjustified?

To hold that none of the company's expenses are to be taken into account, in arriving at the figure for taxable profit, would amount, I think, to holding that the interest on investments was not part of the company's business. It would be the similar thing in the result as taxing the company on its interest on its investments under Section 8 and not in relation to its business under Section 10. To hold, on the other hand, that the whole of the expenses of the company's business may be deducted in full against its interest on investments would be tantamount to holding that the company had no expenses in its insurance side of its business. As at present advised, though this is not part of the question directly referred to us, once it is decided that it is correct in the case of this insurance company to treat the management of its investments as part of its business, and to treat the carrying on of its insurance business even though this arises solely out of mutual receipts and mutual payments also as part of its business, it must follow, in my view, that the total expenses of its business must be shared between the non-taxable part of its business, (that is, its insurance work) and the taxable part of its business, (that is, the management of its investments).

I have taken careful note of the somewhat caustic comments of Lord Davey in *London County Council* v. *Attorney-General*[1], when dealing with the system of apportionment in the class of cases referred to above; where the question was the question of fact whether money had been paid or not out of a particular fund; where he observed: " The contention is that...... ......only a rateable proportion ought to be deemed to be paid out of their income from rents or from interest receivable by them from their own debtors. The proposition has the merit of novelty. Admittedly there is no authority for it. The attention of your Lordships was not called to any statutory enactment directing any such procedure, or to any principle of law which prescribes it. On the contrary, the general principle of payment in due course of administration is to pay annual charges in the first place

(1) [1901] A.C. 26, at p. 46.

out of annual income." Which is the passage also referred to by Pollock, M.R., in the *Sterling Trust case*[1].

I have given anxious consideration to the question whether those comments are equally applicable to such a case as the present where the question is one of the calculation of the amount of profits and (within that) of the amount of expenses to be taken into account in earning the profits before the figure for profits is arrived at. This Court would of course be bound by those observations for the exclusion of any system of proportional calculation if the two classes of cases were the same. I have already observed that in my view the principle of attribution laid down in the class of case being considered by Lord Davey is not applicable in the present case. Lord Davey's remarks regarding the system of proportion were made only in connection with a process of attribution which arose in those cases but does not arise in this case. After giving the matter full consideration it seems to me that those comments are not intended to be applied and are not at all applicable to such a case as the present, where the question is not the source from which certain moneys had in fact been paid or to be deemed to have been paid, but a pure question of calculation of the amount of profits. As at present advised I see no better alternative as a matter both of logic, arithmetic and justice than that the Income-tax Officer in applying rule 25 should adopt a system of proportion; by taking first one-fifth of the surplus shown (by a comparison of the two actuarial reports) which would give the figure for total annual profit if this company had been a non-mutual insurance company; and then taking some proportionate part of that figure so as to arrive at a proper figure representing that part of such total annual figure as would represent the portion of taxable profit in the case of this mutual insurance company. It will be for the Income-tax Officer to divide the figures of the relation in which the proportion should be calculated. Such an assessment though based on valuations on the actuarial reports would have a similar effect as allotting (if an assessment had been carried out under Section 10) a portion of the total expenses of the carrying on of the whole combined business of the company to the earning of the taxable profit.

There should be no practical difficulty that I can see in this.

In regard to the manner in which the questions referred to us should be answered, I agree with my learned brother that the answers should be:—

(1) Does not arise.

(2) In the affirmative.

(3) In the negative.

I would like, however, for myself to add these qualifying or explanatory remarks.

(1) (1925) 12 Tax Cas. 868, at p. 889.

Regarding question No. 2 I understand this question to relate to the year of assessment 1937-38. I wish to reiterate that if rule 25 is to be applied, it will in any event not be the income, profits and gains for the accounting year ending 31st December, 1936, which will be being assessed. No receipts or expenditure shown in that accounting year will at all be taken into account. It will be a notional average annual figure for income, profits and gains for the assessment year 1937-38, which is to be arrived at based on the actuarial report covering the five years between 1st January, 1929, and 31st December, 1934; and the material from which such notional average figure will be calculated will be those five accounting years as reflected in the valuation given in the actuarial report of 1934 read in comparison with the actuarial report of 1929.

Reference answered accordingly.

[IN THE BOMBAY HIGH COURT.]

MOTICHAND AND DEVIDAS, *In re.*

KANIA, AG. C. J., and CHAGLA, J. September 6, 1944.

INDIAN INCOME-TAX ACT (XI OF 1922), SECS. 13, 25 (3)—FIRM OF SOLICITORS—FIRM ASSESSED UNDER ACT OF 1918—DEATH OF PARTNER—NEW PARTNERSHIP BETWEEN REMAINING PARTNERS—USE OF SAME FIRM NAME AND PREMISES—ASSETS AND LIABILITIES NOT TAKEN OVER—WHETHER PROFESSION WAS DISCONTINUED—RIGHT TO RELIEF UNDER SEC. 25 (3)—WHAT CONSTITUTES DISCONTINUANCE OF PROFESSION—RIGHT OF EACH PARTNER TO USE NAME OF DISSOLVED FIRM—METHOD OF ACCOUNTING—SYSTEM OF WITHDRAWALS, WHETHER A METHOD.

The firm of Motichand and Devidas was carrying on the business of attorneys since 1909. The original partners were Motichand and Devidas. In 1936 Tanubhai, son of Devidas, was also taken as a partner. Devidas died on the 8th July, 1940, with the result that the firm was dissolved and a fresh partnership deed was entered into between Motichand and Tanubhai with effect from the 8th July, 1940. As the firm of Motichand and Devidas had been assessed to income-tax under the Act of 1918, in the assessment year 1940 the firm which was in existence up to the 8th July, 1940, claimed relief under Section 25 (3) of the Income-tax Act on the ground that there was a discontinuance of business on the 8th July, 1940. It was found that the new firm had not taken over the outstandings or liabilities of the old firm but started with new books and got fresh retainers from all clients, but the business was carried on in the same firm name and at the same premises:

Held, *that there was a discontinuance of the business of the old firm on the 8th July, 1940, and the assessee was entitled to the relief mentioned in Section 25 (3) of the Act.*

Held, *also, that "withdrawals" by partners is not a method of keeping accounts within the meaning of Section 13 of the Act and the fact that an assessee had been assessed in previous years on the footing of withdrawals in each year cannot make it a method of accounting.*

In the absence of an agreement between the partners, on the dissolution of a firm of solicitors, each partner is entitled to carry on business in the old firm name provided that he does not by his action expose the outgoing partner or his estate to liability for the fresh business.

Where a firm is dissolved by the death of a partner, to constitute discontinuance of the profession of the firm it is not necessary that there should be a giving up of the profession altogether by the remaining partners.

Cases referred to :—

Arundale *v.* Bell [1888] (52 L.J. Ch. 537).

O. Rm. M.S.P.S.V. Meyyappa Chettiar *v.* Commissioner of Income-tax, Madras [1943] (11 I.T.R. 247 ; 56 L.W. 588 ; A.I.R. 1943 Mad. 504 ; (1943) 2 M.L.J. 8).

P. E. Polson, *In re* [1942] (10 I.T.R. 52 ; I.L.R. 1942 Bom. 216 ; 198 I.C. 430 ; 43 Bom. L.R. 1034 ; A.I.R. 1942 Bom. 50).

Reference under Section 66 (1) of the Indian Income-tax Act (XI of 1922) by the Income-tax Appellate Tribunal: (Income-tax Reference No. 26 of 1943).

STATEMENT OF CASE.

"Under Section 66 (1) of the Indian Income-tax Act, 1939, we are submitting this reference to the High Court of Bombay, at the instance of the assessees Messrs. Motichand and Devidas. The reference relates to their assessment to income-tax for the fiscal year 1940-41, in respect of their income, profits and gains of the calendar year 1939 which is their "previous year," *i.e.*, year of account, and arises out of our judgment in their appeal, R. A. A. No. 28-Bombay of 1942-43, to the Income-tax Appellate Tribunal. In their application for reference, marked Exhibit A in the appended list, the assessees have formulated not less than seven questions stated to be questions of law arising out of our judgment for reference to their Lordships, while the Commissioner of Income-tax, Bombay, contends in his written answer, Exhibit B, that only two such questions arise.

2. The material facts are set out in our judgment. It will be however necessary to add a few in this reference in order to help to understand one of the questions raised in the application. Although we have noticed some of them in the course of our judgment, it was not necessary to set them out in detail because the question to which they are material was not raised in appeal before us and is raised in the present application for the first time. We shall accordingly restate the material and undisputed facts briefly and in one place.

3. The assessees are a firm of Solicitors practising in Bombay. In the year of account the firm was composed of three partners, Messrs. Motichand, Devidas and his son Tanubhai. Mr. Devidas died on July 8, 1940, *i.e.*, in the year of assessment. Thereafter the two remaining partners reconstituted themselves into a new firm as from that date. The deed of partnership in this connection came to be engrossed on September 12, 1940.

4. The Income-tax Officer made the present assessment upon the firm as constituted at the date of the assessment and apportioned the total income, which he computed at Rs. 1,05,264, among the three partners, Messrs. Motichand, Devidas and Tanubhai, in accordance with the provisions of Section 26 (1) read with its first proviso. There is no contest as regards the apportionment itself. It will appear from the assessment order that the total income computed by the Income-tax Officer is classified under the following four heads :—

		Rs.
(i)	Income from profession received during the year of account ...	28,000
(ii)	Sale proceeds of the Nanabhai Lane Property and Santa Cruz property sold in the year of account ...	52,500
(iii)	Accumulated depreciation reserve in respect of the Nanabhai Lane property ...	23,000
(iv)	Income from property ...	1,764
	Total	1,05,264

5. Speaking of the computation of the professional income, the method of accounting regularly employed by the assessees is the "receipt" or "cash" method as distinguished from "mercantile" or "accrual" method. Under Section 13 of the Act, income, profits and gains have to be computed for the purposes of Sections 10 and 12 in accordance with the method of accounting regularly employed by the assessees. Section 10 of the Act deals with the computation of income, profits and gains from business, profession or vocation. The assessees' income from the profession of Solicitors had thus to be computed under Section 10 according to the method of accounting regularly employed by them as just pointed out. As a matter of fact, however, the annual assessments in the past used to be made upon the firm in respect of its professional income upon what is called in this case as the "drawing" basis. That is to say, the aggregate of the amounts drawn by the partners out of the firm's profits in the year of account was taken to be the income assessable in the year of assessment. The result was that such portion of the income of the account year left with the firm without being drawn

by the partners did not use to be included in the assessable income chargeable in the year of assessment, and thus remained untaxed. In the present assessment, however, the Income-tax Officer thought that such a basis of assessment was not in accordance with the method of accounting regularly employed by the assessees and therefore computed their professional income at Rs. 28,000 on the "receipt" or "cash" basis.

6. As regards the sale proceeds of the two properties included in the assessment the facts are that the assessee firm owned two buildings, one known as the Nanabhai Lane property, in the Fort area and the other known as the Santa Cruz property, in a Bombay suburb of that name. The first was bought in about 1916, for Rs. 27,000. Between the date of its purchase and the year of account the assessees had spent a large sum over its reconstruction and repairs. Further, since its purchase they used to annually set apart a sum of Rs. 1,000 as depreciation reserve in respect of the property, and in the year of account such reserve had accumulated to Rs. 24,000, including Rs. 1,000 set apart in that year. The other property was bought for Rs. 35,000, but the year of its purchase cannot be ascertained. Now all the money invested in these two properties, as well as the amount annually set apart for depreciation, admittedly came out of the firm's income, *i.e.*, income that had remained with the firm without being drawn by the partners. In other words, it represented untaxed income, profits or gains. This state of things appears to have attracted the attention of the Income-tax Officer in the assessment for the year 1933-34. The assessee firm, however, wrote to him a letter, dated May 16, 1934, material portion of which is reproduced in the Appellate Assistant Commissioner's order. In substance, they offered to bring the sale proceeds of these properties to the tax after their sale when they stated the amount shall be credited to the property account in the firm's books. The Income-tax Officer appears to have agreed to such a course, probably having regard to the peculiar method of assessment described before. In the year of account material to the present assessment the assessee firm sold both these properties to the partners Messrs. Devidas and his son Tanubhai for Rs. 32,500 and Rs. 20,000, respectively, and brought these two amounts as well as the accumulated depreciation reserve to the credit of the property account. The Income-tax Officer included these sale proceeds aggregating to Rs. 52,500 into the present assessment, obviously in pursuance of the assessees' offer contained in their letter just referred to. As regards the accumulated depreciation reserve of Rs. 24,000, the assessees had accounted for Rs. 1,000 set apart in the year of account. The Income-tax Officer therefore added the balance of the accumulation, *viz.*, Rs. 23,000 to the assessees' assessable income. There was no dispute with regard to the income from property. A copy of the assessment order is Exhibit C. The assessees took

the order in appeal to the Appellate Assistant Commissioner who confirmed the assessment. A copy of his order is Exhibit D.

7. The assessees thereafter took an appeal, R. A. A. No. 28-Bombay of 1942-43, to the Appellate Tribunal. From their memo of appeal, a copy of which is Exhibit E, it will appear that they raised only four points. Firstly, they contended that the business of the old firm composed of three partners, Messrs. Motichand, Devidas and Tanubhai, came to be discontinued on the death of Mr. Devidas and consequent dissolution of the firm by operation of law, on July 8, 1940, and that the business that was being carried on thereafter by the reconstituted firm of the remaining two partners was a new business. On this ground, and also because of having been taxed under the Income-tax Act of 1918, they claimed the benefit of Section 25 (3) of the Indian Income-tax Act, 1939, and asked to be exempted from the payment of the tax for the period between the end of the previous year 1939 and the date of the alleged discontinuance, *i.e.*, July 8, 1940; and further asked that the profits of this period be substituted for those of the "previous year." In the alternative, and that was the second ground in appeal, the assessees claimed to have succeeded to the business of the old firm, and on that footing claimed a similar relief provided by Section 25 (4) of the Act. Thirdly, they objected to their assessment on the "receipt basis." And lastly, they objected to the addition of Rs. 23,000, which, as we have just pointed out, was the accumulated depreciation reserve to their assessable income.

8. A copy of our judgment is Exhibit F. Our finding on the first point was that there was no discontinuance of the business of the old firm and that the applicants were carrying on the same business, the change being only in the firm's constitution. Our reasons for the finding are set out in paragraph 3 of our judgment. It is agreed between the two sides that the finding gives rise to a question of law. The applicants have formulated two questions for reference, but we agree with the Commissioner in thinking that the finding raises only one question which we shall set out presently.

9. As regards the second and alternative contention, the learned counsel for the applicants declined to argue the question of succession, although it had been taken in paragraphs 4 and 5 of the memo of appeal. The learned counsel stated that there was no succession in this case as the applicants were not carrying on the business of the old firm.

In consequence, the Advocate-General who appeared for the Crown declined to address us on that point. We have referred to this part of the case in the concluding portion of paragraph 3 of our judgment. Nevertheless, the applicants have raised two more questions, Nos. 3 and 4, on the point of succession for reference to their Lordships. And in this connection it is alleged in paragraph 4 (1) of the present application :—

"The Bench erred in observing that the point as to succession was given up by counsel for the applicants."

In the first place, we must point out that we have nowhere said in our judgment that the question was "given up" by the counsel. We have only stated that the counsel declined to argue the question of succession and that, in consequence, the Advocate-General declared that he was not addressing us on the point. As a matter of fact, the Advocate-General told us that he did not propose to deal with the question of succession under Section 25 (4) as the appellants had abandoned that part of the case. Next, we are constrained to observe that the averment to which we have just referred is not correct in point of fact. We are however content to leave it at that and do not feel inclined to take further notice of the suggestion conveyed by it. As the matter stands, no question of law such as can be referred to the High Court arises out of our judgment on this point for the plain reason that we did not deal with the question and have not recorded any finding on it, in the circumstances just described.

10. The fifth and the sixth questions raised in the present application relate to the assessment being made upon the "receipt" basis instead of the "drawing" basis. We have discussed this part of the case in paragraph 4 of our judgment. We held that the applicants having maintained their accounts according to the "cash" or "receipt" method they could be assessed only according to that method of accounting. It is agreed by both sides that our finding on this point raises a question of law. But that is only one question which we shall set out below.

11. The seventh and last question proposed by the applicants is :—

"Whether in the event of the assessment on cash or receipt basis being upheld, the sum of Rs. 52,500 being the sale price of the two properties, *viz.*, at Nanabhai Lane and Santa Cruz was properly included in the income of the assessee liable to assessment."

Obviously, such a question does not at all arise out of our judgment for reference to their Lordships. The contention involved in the question is that the sale proceeds of Rs. 32,500 in respect of the Nanabhai Lane property, and Rs. 20,000 in respect of the Santa Cruz property, ought not to have been included in the present assessment inasmuch as these proceeds were not income of the "previous year." But no such contention was made in the appeal before us. We have enumerated the only four grounds taken in appeal before us. We have already disposed of three. The fourth and the last was an objection to the addition of Rs. 23,000 which was accumulated depreciation reserve in respect of Nanabhai Lane property. It was contended before us that this amount did not represent the income of the "previous year" which alone could be taxed in an assessment year, under Section 3 of the Indian Income-tax Act. We accepted this contention and

modified the assessment by excluding the amount of Rs. 23,000 from the assessees' assessable income. In this connection we observed towards the end of our judgment :—

"It is quite true that the whole of the sale price of Rs. 32,500 has been included in the previous year's income. We cannot say what might have been the result, if the appellant had raised a similar contention against its inclusion. We refrain from expressing any opinion on the point since the appellant firm has taken no objection to the sale price being so included."

This observation also held good with regard to the remaining Rs. 20,000 representing the sale proceeds of the Santa Cruz property to which also no objection was taken in appeal before us. An explanation is offered as to why the point was not taken. But that does not help to bring into being a point which was never taken. Thus this part of the case was not put in appeal before us and consequently there is no finding. The question therefore does not arise out of our judgment within the meaning of Section 66 (1) of the Act.

12. Therefore, the only two questions that we submit for the opinion of their Lordships are :—

Questions referred.—(1) Whether, in circumstances of the case, there was a discontinuance of the business or profession carried on by Messrs. Motichand and Devidas on July 8, 1940, when Mr. Devidas died, so as to entitle the assessees to the relief provided by sub-section (3) of Section 25 of the Indian Income-tax Act, 1939?

(2) Whether, in the circumstances of the case, the applicants were properly assessed on the "receipts" or "cash" basis?

Taraporewalla, for the assessees.

M. C. Setalvad and *G. N. Joshi*, for the Commissioner.

JUDGMENT.

KANIA, Ag., C. J.—This is a reference made by the Tribunal of Appeal under Section 66 (1) of the Indian Income-tax Act, in respect of the assessment of Messrs. Motichand and Devidas, Solicitors, for the accounting year 1939. The relevant facts are these.

The firm of Messrs. Motichand and Devidas was carrying on business, as attorneys of this Court, since 26th January, 1909. The first partnership deed, referred to in this reference, was dated 29th October, 1926, and was executed between Mr. Motichand G. Kapadia and Mr. Devidas J. Desai, they sharing the profits and loss equally. A fresh partnership deed dated 15th July, 1936, was executed when Mr. Tanubhai, son of Mr. Devidas, was admitted as a partner. The shares of the partners were then re-adjusted, Mr. Motichand got seven annas, Mr. Devidas got seven annas and

Mr. Tanubhai got two annas. The shares of the partners were subsequently changed to seven annas, five annas and four annas respectively, according to the writing dated 20th November, 1937. Mr. Devidas died on 8th July, 1940, with the result that on that day the firm was dissolved. A notice dated 11th September, 1940, was published in the Government Gazette and other newspapers notifying the dissolution of the firm on 8th July, 1940. A fresh partnership agreement was entered into on 12th September, 1940, between Mr. Motichand and Mr. Tanubhai, sharing profits and loss equally, with effect from 8th July, 1940.

The partnership carried on business at different places. On 8th July, 1940, it was carrying on business in a building in Nanabhay Lane. That was originally owned by the partnership but was sold to Mr. Devidas. On 8th July, 1940, the partnership was paying rent to Mr. Devidas for the premises occupied by it. The partnership maintained books of account and in the previous years the partners were assessed on the footing of the amounts withdrawn by them individually. That was taken as their income or profits from the business of the firm. For the assessment year 1940 a question arose about the liability of the firm for its income for the accounting year 1939. On behalf of the assessees it was contended that on the death of Mr. Devidas on 8th July, 1940, the firm was dissolved and its business was discontinued. As the firm of Messrs. Motichand and Devidas was assessed to tax under the Act of 1918, the firm which was in existence up to 8th July, 1940, claimed relief under Section 25 (3) of the Act. On behalf of the Department it was urged that the firm had not discontinued its business, but on the death of Mr. Devidas the other two partners continued the business of the old firm, and therefore no relief under Section 25 (3) of the Act could be given to them. In that connection it was pointed out that when Mr. Tanubhai was admitted as a partner in 1936 there was a change in the constitution of the firm, and if that firm is considered to be the firm which had discontinued its business, that firm had not been assessed to income-tax under the Act of 1918. It was contended that a mere change in the constitution of the firm did not amount to discontinuance of the business of the old firm and relief under Section 25 (3) was not permissible under the circumstances. In respect of the amount for which the firm was liable to be assessed, it was urged by the Department that withdrawal is not "a method of keeping accounts" under Section 13 of the Act, and under that section withdrawal could not be considered a method of accounting regularly employed by the assessees. To put it at its highest it may be considered a rough and ready method of ascertaining their profits, but in no event can it be considered a method of accounting. Under the Act only two methods are recognised as methods of accounting, *viz.*, mercantile method and "receipts" and "cash" basis. As the amounts withdrawn

do not amount to a method of accounting, the Income-tax Officer was entitled to adopt the "cash receipts" method in assessing the income. On these facts the Tribunal has referred the following two questions for the Court's opinion: (1) Whether, in the circumstances of the case, there was discontinuance of the business or profession carried on by Messrs. Motichand and Devidas on 8th July, 1940, when Mr. Devidas died, so as to entitle the assessees to the relief provided by sub-section (3) of Section 25 of the Indian Income-tax Act, 1939? (2) Whether, in the circumstances of the case, the applicants were properly assessed on the "receipts" or "cash" basis?

Dealing with the second question first, it appears to us clear that the Income-tax Officer was entitled to adopt the method of receipts or cash basis, for assessing the income of the assessee firm. The fact that they had been assessed in the previous years on the footing of their withdrawals in each year, cannot make it "a method of accounting regularly employed by the assessee" as it was not a method of accounting at all. In practice, this should not work any injustice on the assessees because if they have not withdrawn the amounts in one year towards profits, they would withdraw it in another year. On the other hand, it must be conceded that withdrawals are not the test of profits. Under the Act the question is what is the total income of the assessees? The answer that Rs. so many were withdrawn by the partners is not an answer in accordance with the Act. The profits or income of a Solicitor's firm, speaking broadly, are the profit costs of the firm, after defraying their expenses of keeping their office. For instance if in a particular year the firm had completed 200 transactions of conveyancing and received the profit costs for the work from their clients, the profits would be received in that year and earned in that year. If for any reason the partners did not consider it necessary to withdraw money from the firm during that year, it will be wrong to contend that the profits of the year were not the profit costs received by the firm during that year. It seems therefore that the conclusion of the Tribunal that the Income-tax Officer was right in adopting the receipts or cash basis for ascertaining the income or profits of the firm is correct. The answer to the second question is in the affirmative.

The first question falls into two parts. The first part is the question of construction of Section 25 (3) as read with Section 26 of the Act. On behalf of the Commissioner it was urged that discontinuance of the business or profession or vocation must mean a cessation of that business, as the word "discontinuance" is ordinarily explained in dictionaries. It was contended that a change in the constitution of the firm did not amount to a discontinuance. It was argued that if the owner of a business was A

and he sold the business to B the business still continued, and although relief may be available under Section 25 (4), on the ground of the assessee succeeding to the business of the previous assessee, no relief could be granted under Section 25 (3), because for that purpose the relevant question is " has the business been discontinued ? " The argument is that under Section 25 (3) the point for consideration is not, who is the assessee, who was doing business, but has the business continued or discontinued. In *In re P. E. Polson* [1], our High Court has held that if a business carried on by A was sold to B, if A had paid income-tax under the Act of 1918 he was entitled to get relief under Section 25 (3). That case has been doubted in *O. Rm. M. SP. S. V. Meyyappa Chettiar* v. *Commissioner of Income-tax, Madras* [2]. I appreciate that there is force in the reasoning of the Madras case. We are however bound by the decision in *Polson's case*[1] and it is possible to decide the present reference without going into this question of law. I do not propose to discuss it any more.

The second part of the question is : " Has there been a discontinuance" in the narrow sense of the word? The question of law which has to be decided in that connection is whether on the facts admitted or proved the firm of Messrs. Motichand and Devidas, which was in existence on 8th July, 1940, has discontinued its business. In my opinion a discussion as to whether the firm of Messrs. Motichand and Devidas which came into existence after 8th July, 1940, has succeeded to the business previously carried on by the firm in existence up to that date is not relevant for this discussion. That discussion would be relevant if relief was claimed under Section 25 (4) read with Section 26 (2). For the purpose of the present discussion the only question is whether the business of the old firm had been discontinued. I have already summarised at the commencement, the facts which are noticed in the judgment of the Appellate Commissioner. The further relevant facts to which our attention has been drawn are these. The new firm did not take over the business as a going concern. No outstandings or liabilities of the old firm were taken over by the new firm. The new firm had started with new books and because the partners in the new firm were two out of the old firm they also worked to wind up the affairs of the old firm. The business carried on after 8th July, 1940, was carried on in the name of Messrs. Motichand and Devidas which was the name used by the old firm, and was carried on in the same premises in which the old firm had carried on business. In their judgment the Tribunal have stated as follows :—

" There is no disposal by assignment or otherwise in the present case. All that has occurred is that two partners of the old firm have reconstituted themselves into a new firm and are carrying on the business or profession

(1) [1942] 10 I.T.R. 52. This case was reversed by the Privy Council ; See [1945] 13 I.T.R 384,
(2) [1943] 11 I.T.R. 247.

which the old firm did, although under fresh retainers, in the same style, in the same premises and in the same manner as before. On these facts, therefore, we do not think that the business of the old firm is discontinued."

The question is whether on the facts mentioned above the business of the old firm has discontinued.

The point of business being done in the same name may be taken first. In *Arundale* v. *Bell*[1], the partners of a firm of Solicitors agreed that the partnership should be dissolved, that two of them should continue to carry on partnership business and should employ the third as a clerk, and that all the books, papers and other properties of the firm should vest in and be the property of the two continuing partners. The third partner died and on behalf of his estate a claim was made on the ground that the firm name was being used by the continuing partners. The claim was on the ground of goodwill. The Court rejected the claim. Jessel, M. R., observed that as a general rule and in the absence of express contract there was not in a partnership between Solicitors any partnership asset which was capable of being sold or valued as the goodwill of the partnership business. The other Lords Justices agreed with the conclusion mentioned above. Mr. Setalvad had relied on the statement of law found in Halsbury's Laws of England, Vol. 31, page 285, where it is stated *inter alia*, that the goodwill is asset in the hands of the administrator, who may assign it for value and it can be disposed of by will, or on the death of one of several partners may pass, subject to the provisions of the articles, to the surviving partners. In support of that statement several cases decided in 1830 and 1850 are relied upon. *Arundale* v. *Bell*[1] is a later decision and deals with the neat point whether a Solicitors' firm as such has a goodwill in the name of the firm, apart from special stipulations and agreement between the parties. In my opinion, the principle as regards the goodwill of a Solicitors' firm as set out in that judgment applies to this case before us. It is also clear in law that upon the dissolution of a partnership between Solicitors, without any sale or assignment of the goodwill of the business, and without any provision as to the use of the firm name, each of the partners is entitled to carry on business in that name, provided that he does not by so doing expose his former partners to any risk or liability, which must depend upon the circumstances of the case. It is therefore clear that in the absence of any agreement between the parties, on the dissolution of the firm, each partner is entitled to carry on business in the name of the old firm. The only limitation to that right is that he should not by his action expose the outgoing partner or his estate to liability for the fresh business. Therefore, the fact that the two partners continued to use the name of Messrs. Motichand and Devidas after 8th July does not prevent the business of the old firm being discontinued.

(1) (1883) 52 L.J. Ch. 537.

The question of the business being carried on in the same premises, in my opinion, is equally immaterial. Ordinarily, that fact has to be taken into account in considering the goodwill of a business. Apart from that, I do not know of any case in which the fact that the business was conducted in the same place as before was considered relevant. In any event, the premises here were rented premises, and the evidence does not show that the occupation of the premises carried with it any connection with the old business of Solicitors.

The statement of the Tribunal in their judgment that the business of the Solicitors was carried on in the same manner does not convey anything in particular. The business of the firm was conducted by three Solicitors. It was the firm that was doing business. So long as the individual partners are Solicitors, any business done by them as Solicitors must be in the same manner. To put it in other words a Solicitor's business, whether conducted by an individual or with others in partnership, must be conducted in the same manner. It was argued that in interpreting Section 25 (3) when the question arises in respect of the business of a firm of professional men, the business could be considered discontinued only when the partners constituting the firm started an altogether different kind of business, *e.g.*, instead of working as Solicitors they started a business of stock-brokers or dealers in cotton. In my opinion, there is no justification for going to that extreme and in the absence of authority I do not accept that argument.

In the present case it is admitted that fresh retainers were taken by the new firm. A retainer is nothing more than an authority given by a principal to the agent. On the change in the partnership firm, as the firm will be a new firm, that is different from what it was before, in law, there would be a different agent and therefore a fresh retainer will be necessary. That fact however does not affect the answer to the question whether there has been discontinuance or not. In the present case there is nothing to show that anything which belonged to the old firm had been continued after 8th July, 1940, except for the purpose of winding up the affairs of the old firm. The fact of new retainers being given indicates that the clients had intimation that the business of the old firm had come to an end and if they wanted to employ the new firm fresh contracts had to be executed. In the matter of a professional partnership a question arises, what is the business? On the footing that business is a series of transactions involving giving something by one party in consideration of something being given by the other party, a professional partnership gives the benefit or use of its professional knowledge and experience to the client in consideration of the client paying the charges. The client is entitled to the benefit of the knowledge and experience of the partners, and if that is incapable of being given after a

particular date, it seems to me that there must be discontinuance of the business. It was argued on behalf of the Commissioner that this conclusion would mean that in every case when there is a change in the partnership there is a discontinuance of the business. I do not think that conclusion naturally follows. As an illustration, in this very case, when Mr. Tanubhai was admitted in partnership, in my opinion, it cannot be contended that the business of the old firm had discontinued. That firm continued, as a going concern, the business of the old firm. The clients became entitled to the knowledge and experience of the new partner, in addition to the knowledge and the experience of the so far existing partners. There is thus a clear distinction between "discontinuance" of a business and a "change" in business. Section 25 (3) does not deal with a change in the business. It deals with the contingency of discontinuance of the business. Applying another test to the facts here, it is clear that when Mr. Tanubhai was admitted as a partner, as required by the Partnership Act, notice was given to the Registrar of Firms, intimating that there was a change in the partnership. After 8th July, 1940, when Mr. Motichand and Mr. Tanubhai did business in the name of Messrs. Motichand and Devidas, they did not intimate that there was a change in the old firm, but they filed a fresh application for the registration of the new firm, which thereafter transacted the business of Solicitors in that name. As I am unable to find anything which shows that the business carried on by the old firm had been kept as if in a chain by the firm which came into existence after 8th July, in my opinion, the business of the old firm was discontinued from 8th July, 1940, and the assessees are entitled to the relief mentioned in Section 25 (3) of the Income-tax Act.

In considering equities I must point out that any other view would lead to the detriment of Mr. Devidas's estate. Mr. Devidas had paid income-tax on the profits of the firm under the Act of 1918. If no relief is granted under Section 25 (3) his estate will be paying double tax in respect of the assessment year. I do not think that should be allowed unless the words of Section 25 (3) clearly prevent the relief being granted. I would therefore answer the first question in the affirmative.

CHAGLA, J.—I agree. In *In re P. E. Polson*[1], our High Court has given a more extensive meaning to the expression "discontinued" in Section 25 of the Act than the Madras High Court has done in *Meyyappa Chettiar* v. *Commissioner of Income-tax, Madras*[2]. But, for the purpose of this reference, we have agreed to accept the narrower construction of that expression which Mr. Setalvad for the Commissioner has contended for. On that narrower construction the question which arises for our determination is whether on the death of Mr. Devidas on 8th July, 1940, there was cessation

(1) [1942] 10 I.T.R. 52. (2) [1943] 11 I.T.R. 247.

of the business of Messrs. Motichand and Devidas carried on before that date. Now it is important to note that in this case the facts are very significant. The new firm of Messrs. Motichand and Devidas did not take over the business of the old firm as a going concern with all its assets and liabilities. No assets were taken over by the new firm and the new firm did not make itself liable for any debts of the old firm. As a matter of fact the new firm opened new books of account and as has been pointed out in the judgment of the Tribunal retainers of the clients of the old firm came to an end. The only importance which I attach to this fact, *viz.*, that the retainers of the clients came to an end is that the new firm did not take over the clients of the old firm and it was open to the clients of the old firm to engage the services of the new firm or not as they pleased. Therefore on the facts it is clear to my mind that there was no nexus whatever between the old and the new firms. The only two facts on which Mr. Setalvad relies are that the new firm carried on business in the same name and at the same place as the old firm. As the name of Messrs. Motichand and Devidas carried with it no goodwill and was not an asset of the old firm the mere fact of the two surviving partners using that name is not material. As regards the place it was a rented premises and that by itself does not in any way help the contention of Mr. Setalvad.

Mr. Setalvad has really contended that under Section 25 (3) the discontinuance of a profession means and must amount to the giving up of a profession, *i.e.*, the changing over of one profession for another. Therefore according to him unless and until the surviving partners in the firm of Messrs. Motichand and Devidas, *viz.*, Mr. Motichand and Mr. Tanubhai ceased to practise as Solicitors, in law there cannot be a discontinuance of the profession. Unless there is some authority which is binding on me I am not prepared to place that construction upon that expression in Section 25 (3). Even the case of *Meyyappa Chettiar* v. *Commissioner of Income-tax* [1] does not go to that length. I therefore agree that the first question should be answered as suggested by the learned Chief Justice.

With regard to the second question I have nothing further to add to what is stated by the learned Chief Justice in his judgment.

P. C.—Having heard counsel on the question of costs and bearing in mind the time spent in the arguments on points which each side has lost and won we order that the Commissioner should pay half the costs of the reference.

Reference answered accordingly.

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(1) [1943] 11 I.T.R. 247.

[IN THE BOMBAY HIGH COURT.]

YAKUB VERSEY LALJEE AND ANOTHER

v.

COMMISSIONER OF INCOME-TAX.

STONE, C.J., and KANIA, J. September 19, 1944.

INDIAN INCOME-TAX ACT (XI OF 1922), SEC. 41 (1), PROVISO—CONSTRUCTION—TRUST DEED—INDIVIDUAL SHARES NOT DETERMINABLE—ASSESSMENT AT MAXIMUM RATE—MEANING OF "OR".

In the first proviso to Section 41 (1) of the Indian Income-tax Act the word "or" must be read as equivalent to "and". Further, the use of the words "individual shares" imposes a consideration of the subject matter as well as the quantum of the shares; so that it has to be determined not only what is the quantum of the share but also who is the beneficiary who is entitled to it and the test for the application of the said proviso is whether both the shares and the beneficiaries who are to take the same are not indefinite or unknown.

[On the construction of the trust deed in question their Lordships held that the income sought to be assessed could not be predicted to belong to any particular individual and was therefore assessable at the maximum rate under the proviso to Section 41 (1)].

Reference under Section 66 (1) of the Indian Income-tax Act (XI of 1922) by the Income-tax Appellate Tribunal: (Income-tax Reference No. 1 of 1944).

STATEMENT OF CASE.

"This is an application under Section 66 (1) of the Income-tax Act, requiring the Tribunal to refer to the High Court certain questions of law arising out of the Tribunal's order in R.A.A. No. 268 (Bombay) 1942-43.

2. For the assessment year 1941-42, the Income-tax Officer assessed the income from the trust created by Yakub Versey Laljee in the hands of the trustees at the maximum rate in terms of the first proviso to Section 41 (1) of the Act. The assessee objected to this treatment and appealed to the Appellate Assistant Commissioner, who rejected the appeal by his order, dated 10th December, 1942. An appeal was then preferred to the Appellate Tribunal and a reference as arising from the Tribunal's order dismissing the appeal is now being sought.

3. The only point in dispute before the Tribunal related to the construction of the trust deed dated 18th September, 1940. The Tribunal found on a true construction of the trust deed that while the shares of the beneficiaries in the trust income are neither indeterminate nor unknown

the income itself is not specifically receivable on behalf of any one person, within the meaning of the first proviso to Section 41 (1). The reasons for this finding are set out in the Tribunal's order made under Section 33 (4) of the Act.

4. We are of the opinion that out of these findings the following question of law arises, which we refer under Section 66 (1) to the High Court of Judicature at Bombay :—

'Whether tax on the income of the trust property or any part of such income is leviable at the maximum rate under the first proviso to Section 41 (1) of the Income-tax Act?' "

The facts of the case and the opinion of the Appellate Tribunal, as set out in the judgment of the Tribunal delivered under Section 33 of the Income-tax Act, were as follows :—

"The trustees of the Yakub Versey Trusts, who are the appellants in this case, object to the income of the trust being assessed at the maximum rate under the first proviso to Section 41 (1) of the Income-tax Act.

2. The trust was created by Yakub Versey Laljee on 18th September, 1940. The settlor directed the trustees by clause 5 of the trust deed, to accumulate the income from the trust property, subject to an allowance to his wife for the maintenance of the settlor's family, till the attainment of majority by the youngest son. By clause 6 certain provisions were made for the marriages of the daughters and the funeral expenses of deceased children, which were to be met from the corpus of the trust's estate. By clause 7, it was provided that on the attainment of majority by the youngest son the corpus of the trust property was to be realised and subject to certain payments, be divided equally amongst the sons of the settlor, who were also to receive the accumulated balance of the trust income in equal shares by virtue of clause 5 of the trust deed.

3. The Income-tax authorities consider that the above-mentioned clauses of the trust deed leave the shares of the beneficiaries in the accumulated income indeterminate and unknown. They have also taken the view that in any case the income of the trust properties is not specifically receivable by the trustees on behalf of any one person in terms of the first proviso to Section 41 (1). The abovementioned provision lays down that unless both these conditions are fulfilled, *viz.*, (i) specifically receivable on behalf of any one person, and (ii) the individual shares of the persons on whose behalf they are receivable are determinate or known, the tax on the income shall be levied at the maximum rate.

4. Clauses 5, 6 and 7 of the trust deed, in our opinion, leave no room for doubt that the shares of the settlor's sons, who are the sole beneficiaries in the accumulated balance of income, payable at a specified time, are clearly defined. The moneys to be paid to the daughters on their marriages

and the provision for funeral expenses etc., are to be met from the trust premises and not from the trust income. Similarly, the gift of Rs. 7,000 to the wife at the time of realisation of the trust properties is to be met from the corpus and not from the income. We find, therefore, that the shares of the beneficiaries in the trust income are neither indeterminate nor unknown within the meaning of the first proviso to Section 41 (1).

5. The second condition, however, that the income should be specifically receivable on behalf of any one person, is not, in our opinion, fulfilled. It is not a case where the trustees are merely to collect and to distribute. The trustees in this case have carefully to nurse the accumulations and on the happening of a specific event, divide and hand over the proceeds in accordance with the terms of the trust deed. In these circumstances the assessees cannot escape from the application of the first proviso to Section 41 (1). The appeal is, in the result, dismissed."

G. N. Joshi, for the assessees.

M. C. Setalvad, for the Commissioner.

JUDGMENT.

STONE, C. J.—This reference, which is made under Section 66 (1) of the Income-tax Act, raises a short point involving the construction which is to be put upon a settlement dated 18th September, 1940, and the application to it of Section 41 of the Act. The settlement is a voluntary settlement made by a father for the benefit of his wife, his four sons and three daughters. It is a settlement of real estate with a power to convert it and invest the proceeds of sale. Clause 3, which contains a definition of the trust premises, is in these terms :—

"In consideration of the premises the trustees hereby covenant with the settlor that they the trustees shall stand possessed of the said land hereditaments and premises described in the Schedule hereunder written and hereinbefore expressed to be hereby granted conveyed transferred and assured and the net sale proceeds thereof if and when sold and the investments for the time being representing the same (all which said premises the net sale proceeds and the investments are hereinafter for brevity's sake called 'the trust premises') and the income thereof..."

Then the paragraph goes on to set out the different trusts. Clause 5 is the clause which deals with the income and after providing that the trustees shall collect the income and pay out of the gross income certain expenses, it continues as follows :—

"......and shall subject to the payments aforesaid pay every month out of the said net income profits or dividends a sum equivalent to 60 per cent. of the net income but not exceeding Rs. 400 to the said Yakub Versey Laljee to be utilised and spent by him for the maintenance of his wife and

for the maintenance, education and other comforts of his said children (whom he mentions by name) and to accumulate and invest the surplus until the youngest of the said sons Ramzanally who is at present of age 5 years shall attain the age of 21 years..."

Clause 6 provides for the daughters' marriage portions and the next clause provides for the ultimate distribution and is as follows:—

"It is hereby further agreed and declared that on the said youngest son of the settlor attaining the age of 21 years the trustees shall realise the trust premises and pay thereout Rs. 7,000......(to the wife of the settlor) and subject to the provision of clause 6 (*i.e.*, daughters' portions) set apart such sum or sums as may be necessary to yield as income at least Rs. 25 for the maintenance education and other comforts of such of the said (daughters) who may then be unmarried and shall then divide and distribute the rest and the remainder of the trust premises amongst his said sons......(who are named in the clause) as tenants in common absolutely in equal shares."

What is to be divided is the trust premises and nothing is stated about any distribution or the destination of the accumulations already directed to be made of the surplus income under clause 5. The only other clause which it is necessary to refer is clause 8:

"Provided always and it is hereby agreed and declared that in the event of all the sons of the settlor dying without leaving any widow them or him surviving before the said youngest son of the settlor attains the age of 21 years the trustees shall give and divide the trust premises and the accrued income thereof among such person or persons and in such manner or proportions as the settlor shall by will or deed appoint and in default of such appointment and to the extent that any such appointment fails among the heirs of the settlor as on intestacy."

In the ultimate contingency of all the four sons dying without leaving widows or heirs what is to be dealt with is the trust premises and the accrued income thereof. Now it is suggested by Mr. Joshi that the "accrued income" is included in the accumulations, and, therefore, is undisposed of. In my opinion that is not so. Although in my judgment, the accumulations are undisposed of and go to the settlor under a resulting trust, the income does not become "accumulations" until the trustees have dealt with it by investing it pursuant to clause 5, and uninvested income remains "accrued income." If that is so, it cannot be predicted who is so entitled to the accrued income unless and until the settlor has executed an irrevocable deed appointing himself or somebody else to whom the accrued income is to go if the contingency of the four sons dying before the youngest son attained 21 years of age should happen. It has not been seriously suggested that the income

with which we are dealing, *viz.*, Rs. 2,071 is not "accrued income" but is an accumulation under clause 5 because this Rs. 2,071 is in fact uninvested income of the current year. Now that being the position and the construction which in my opinion should be put upon the document it is now necessary to look at Section 41.

The object of the section is to provide for the taxation of income which arises under trusts. Sub-section (1) directs that tax shall be levied upon and recoverable from Courts of Wards, Administrators-General, Official Trustees, or any receiver or manager or any trustee or trustees, in the like manner and to the same amount as it would be leviable upon and recoverable from the person on whose behalf such income, profits or gains are receivable and all the provisions of the Act shall apply accordingly. That is a benefit to the tax-payer because except for it tax would have been leviable on the income in the hands of the trustees at the maximum rate but you have to ascertain the beneficiary, and the tax leviable is at the rate payable by the beneficiary as if this trust income was added to his other income. But to that section there is this proviso, *viz.*,

"Provided that where any such income, profits or gains or any part thereof are not specifically receivable on behalf of any one person, or where the individual shares of the persons on whose behalf they are receivable are indeterminate or unknown, the tax shall be levied and recoverable at the maximum rate."

In the first place in spite of the use of the word "or" in that proviso it is my opinion that "or" in this context must be read conjunctively. There can be no point in having the two alternatives unless read as conjunctive ancillary to income, profits or gains not being specifically receivable on behalf of any one person. But the difficulty in this case is caused by the second limb of this proviso. What is it which it is postulated may be indeterminable or unknown? The answer must be, the individual shares of the persons on whose behalf the income is receivable. If the word "individual" did not appear before the word "shares" I think there would be little doubt that it would be quantum of the shares and not the identity of the beneficiary to which reference was being made. But the words of the statute are "individual shares" and in my judgment that imposes a consideration of the subject-matter as well as the quantum. So that it has to be determined not only what is the quantum of the share but also who is the beneficiary who is entitled to it, and the test must in my opinion be whether both the shares and the beneficiaries who are to take the same are not indefinite or unknown. Now applying that test in this case to the sum of Rs. 2,071 the answer must be that as there has been no irrevocable appointment under clause 8 it cannot be predicted what the ultimate destination of this accrued income might be because in the

unlikely event of all the sons being killed in some common accident the accrued income which for the present purpose is the sum of Rs. 2,071 might have gone either as income undisposed of by the father or as it might be appointed by him. In any event the matter is uncertain. That being so in my opinion it comes within the proviso and tax is recoverable at the maximum rate.

KANIA, J.—I agree. We are concerned in this reference with the accounting year 1940-41. In the income in question, the 40 per cent. directed to be accumulated under the trust deed, the material provisions of which have been summarised in the judgment of the learned Chief Justice, is included. Having regard to the definition of the "trust premises" in clause 3 a perusal of clauses 5, 6 and 7 shows that the settlor, while directing the 40 per cent. of the income and the surplus of 60 per cent. over the amount of Rs. 400 to be accumulated, has not directed how that accumulation is to be disposed of when the youngest son attains the age of 21 years. Clause 8 contains a proviso in which the words "accrued income" are used along with the words "trust premises." Reading that clause as a whole, it appears therefore that on the happening of the contingency therein mentioned the trust premises and the accrued income are to be dealt with and disposed of by the trustees in accordance with the directions which may be contained in any will or deed executed in exercise of the power of appointment retained by the settlor or in default of such appointment, or to the extent the appointment fails, among the heirs of the settlor as on intestacy. According to the wording of that clause on the happening of the contingency therein contemplated, the heirs of the settlor also get the accumulated income only by virtue of that clause in the trust deed. The power of appointment reserved by the settlor does not inure for the benefit of any heir, if the settlor chooses to make the appointment in his favour, till the appointment is made. Therefore, it is clear that whilst under clauses 5, 6 and 7 the accumulated income is not disposed of, the same does not become the property of the settlor until the contingency contemplated in clause 8 occurs.

On the statement of the case it is clear that in the accounting year the income remained in the hands of the trustees without acquiring the character of accumulated income. It is equally clear that on the facts, so far no steps have been taken to make the contingency contemplated in clause 8 occur, in respect of the income which has accrued in the accounting year. The question before the Court is necessarily in respect of the accounting year only and does not affect the rights of the parties in respect of the income which may accrue in a later year. Having regard to the facts found on the construction of the clause it is clear that within the meaning of Section 41 proviso (1), in the accounting year the income cannot be

predicted to belong to a particular individual, or if more than one with their determinate specific individual shares. Under the circumstances the proviso applies and the maximum rate is correctly charged. I agree that in the proviso the word "or" has the meaning of "and", otherwise the two parts would be meaningless. In my opinion, therefore, the question submitted for the Court's opinion should be answered in the affirmative. I have already stated that the answer is limited to the income of Rs. 2,071 in the accounting year 1940-41.

P. C.—The assessees to pay the costs of the reference.

Reference answered in the affirmative.

[IN THE SIND CHIEF COURT.]

COMMISSIONER OF INCOME TAX, BOMBAY

v.

JHAMANDAS DEVKISHENDAS.

DAVIS, C. J., and THADANI, J. February 18, 1946.

INDIAN INCOME-TAX ACT (XI OF 1922 BEFORE AMENDMENT IN 1939), SECS. 2 (1) (a), 4 (1) & (2)—AGRICULTURAL INCOME—LAND SITUATED IN INDIAN STATE—PRODUCE BROUGHT TO BRITISH INDIA AND SOLD THERE—INCOME, WHETHER "RECEIVED" IN BRITISH INDIA—WHETHER AGRICULTURAL INCOME—ASSESSABILITY.

The assessees, a firm consisting of 3 partners resident in British India and carrying on business in British India, obtained a lease of agricultural land situated in an Indian State. They brought the produce of the land in its raw and unprocessed state to British India and sold it there: Held, *that the profits were received in British India within the meaning of Section 4 (1) of the Indian Income-tax Act and the assessees were assessable to British Indian income-tax in respect of those profits.* Held, *also, that the profit derived by the sale was not agricultural income within Section 2 (1) (a) of the Act as the land was situated outside British India.*

For the purposes of Section 2 (1) (a) land assessed to land revenue in British India or subject to a local rate must be land in British India.

Obiter: *A local rate within the meaning of Section 2 (1) (a) is a rate imposed for the benefit of the local authority or local area as distinct from taxes forming part of the revenue of a Provincial Government.*

Cases referred to:

Chellappa Chettiar, S. A. S. S. *v.* Commissioner of Income-tax, Madras [1937] (5 I.T.R. 97; I.L.R. [1937] Mad. 734; 168 I.C. 160; A.I.R. 1937 Mad. 393; 10 I.T.C. 181).

Commissioner of Income-tax, Madras *v.* S. L. Mathias [1939] (66 I.A. 23; 7 I.T.R. 48; 41 Bom. L.R. 157: 178 I.C. 906; A.I.R. 1939 P.C. 1; I.L.R. [1939] Mad. 178).

Malik Sir Umar Hayat Khan v. Commissioner of Income-tax, Punjab [1925] (2 I.T.C. 52).
Mohanpura Tea Company, Ltd., *In re* [1937] (I.L.R. [1937] 2 Cal. 201 ; 5 I.T.R. 118 ; 10 I.T.C. 218 ; 174 I.C. 488 ; A.I.R. 1938 Cal. 148).

Reference under Section 66 (3) of the Indian Income-tax Act (XI of 1922) by the Commissioner of Income-tax, Bombay, Sind and Baluchistan: Reference (Income-tax) No. 65 of 1942.

STATEMENT OF CASE.

"Statement made under Section 66 (3) of the Indian Income-tax Act, 1922 (hereinafter referred to as "the Act") in respect of the assessment of Messrs. Jhamandas Devkishendas of Shahdadkot (hereinafter referred to as "the assessees") for the year 1937-38.

Facts of the case.—The assessees are a firm consisting of three partners resident in British India who carry on a commission business at Shahdadkot in the Larkana District. They also entered into an agreement with H. H. the Khan of Kalat by which they obtained a lease of certain agricultural land in the Magsi Ilaqa of Kalat State. A copy of the agreement, which is dated the 8th of May, 1935, is annexed and marked A. The provisions which have some relevance to the questions now at issue can be briefly stated as follows:

Clause 1: The lessees will remain in possession of the land for a period of three years from the 16th of June, 1935, with an option to extend the period by a further two years.

Clause 2: The lessees agree to pay as consideration for the lease a sum of Rs. 51,000 annually.

Clause 3: The lessees will be competent to bring the whole of the leased land or any part thereof under cultivation of any kind excepting rice, subject to the conditions, rules etc., required or imposed by the Sukkur Barrage canals authorities.

Clause 7: The revenue assessment and water rate will be paid by the lessor, the lessees "being only bound to pay the lessor a net sum of Rs. 51,000 annually and nothing more."

Clause 9: It is the duty of the lessor to provide sufficient water supply for the cultivation of the leased land to the extent permitted by the canal authorities and for this purpose to make full and timely arrangements with the Baluchistan and Bombay Governments, but in case the lessees cultivate more land than is permissible from time to time they will be liable to pay all dues or fines imposed in respect of such excess cultivation.

Clause 11: The lessees will not be liable for payment to the lessor or Kalat State of any tolls or transit duties on any grain imported for cultivation into the Magsi Ilaqa or other goods imported for their personal use or on the export of the produce of the leased land in British India.

Clause 13: The lessor undertakes not to levy for his own benefit or for the State any new cess, tax or duty upon the cultivators of the lessees.

2. The assessees also produced before the Income-tax Officer the following documents:

(1) Memorandum dated the 23rd of July, 1936, from the Wazir-i-azam, Kalat State, to the Revenue Officer, Magsi Ilaqa Jhal, showing that one-tenth of the total demand was due to the State on account of land revenue and nine-tenths due to Government on account of water rate.

(2) A receipt from the Magsi Sardar for the amount shown in item (1), and

(3) A memorandum from the Revenue Officer, Ilaqa Jhal, to the assessees regarding the amount payable by them under clause 9 of the agreement in respect of excess cultivation.

Copies of these documents are annexed and marked B, C and D respectively.

3. The assessees brought the agricultural produce of the leased land in its raw state to Shahdadkot in the Larkana District and sold it there. The sales effected during the relevant accounting period resulted in net profit of Rs. 84,714. The Income-tax Officer, Larkana, held that this profit was liable to income-tax. He therefore added it to the income from the commission business and made an assessment on a total income of Rs. 90,000. The assessees appealed against this assessment to the Assistant Commissioner of Income-tax, Sind and Baluchistan, but he confirmed the order passed by the Income-tax Officer. Copies of the assessment and appellate orders are annexed and marked E and F respectively.

4. The assessees then submitted an application under Sections 33 and 66 (2) of the Act requesting the Commissioner to review the assessment or in the alternative to make a reference to the Chief Court on certain questions of law. A copy of their application is annexed and marked G. My predecessor however declined to interfere with the assessment and also held that there was no necessity for a reference. Copies of his orders are annexed and marked H and I respectively.

5. *Questions for decision.*—Being dissatisfied with my predecessor's decision the assessees applied to the Chief Court under Section 66 (3), and it was agreed between the parties that the following questions should be referred for the decision of the Court:

(a) Where a resident of British India who has business in British India takes a lease of agricultural land in an Indian State and brings the crop into British India where it is sold, does the profit arise in British India?

(b) If the answer to the above question be in the affirmative, is the profit in the circumstances of the present case agricultural income in

British India within the meaning of Section 2 (1) (a) of the Indian Income-tax Act?

6. *Opinion of the Commissioner.*—In connection with the first question I respectfully invite a reference to the decisions of the Calcutta High Court, *Port Said Salt Association Ltd.* v. *Commissioner of Income-tax, Bengal*[1], and *Mohanpura Tea Company Ltd.* v. *Commissioner of Income-tax, Bengal*[2], where it was held in similar circumstances that the income accrued or arose in British India since the produce was sold there. In the earlier of these cases Rankin, C. J., remarked that 'profit, though it may be anticipated by valuation or otherwise, is not realised before price, and when the article is sold the whole profit is realised for the first time.' It is true that these rulings were not followed by the Madras High Court in the case of *Diwan Bahadur S. L. Mathias*[3]. That case however was subsequently taken to the Privy Council[4] and although their Lordships gave no definite finding on the question whether the income accrued or arose in British India they held that it was in any case received in British India, and was therefore taxable under Section 4 (1). I submit that this ruling is applicable to the present case also. Even if the income in question did not accrue or arise in British India it was undoubtedly received in British India and is liable to tax on this basis.

7. As regards question (b) the definition of 'agricultural income' given in sub-section (1) of Section 2 reads as follows:—

'any rent or revenue derived from land which is used for agricultural purposes, and is either assessed to land revenue in British India or subject to a local rate assessed and collected by officers of the Crown as such.'

The land in question is not in British India, but a water rate is payable to the Baluchistan authorities for water supplied from the Sukkur Barrage. The assessees contend that this water rate should be considered either as land revenue or as a local rate for the purpose of the definition.

8. It seems to me that land revenue and water rates are clearly distinguishable. Land revenue is payable, irrespective of services rendered, to the Government holding jurisdiction over the area in which the land is situated, whereas water rates are payments for specific services received from the authority supplying the water. One of the documents produced by the assessees (Exhibit B) brings out this distinction and shows separately the amount payable to the State in respect of land revenue and the amount payable to the British Indian authorities in respect of water rate. Moreover the fact that a water rate is recoverable as an arrear of land revenue in case of default clearly does not mean that it is itself a part of the land revenue. As my predecessor pointed out in his order, if this argument were accepted income-tax might also be held to be land revenue for the same reason.

(1) (1932) 6 I.T.C. 123.
(2) [1937] 5 I.T.R. 118; 10 I.T.C. 218.
(3) [1937] 5 I.T.R. 435.
(4) [1939] 7 I.T.R. 48.

9. There remains the question whether the water rate can be regarded as a local rate. The term 'local rate' does not appear to have been defined in any enactment, but I submit that in the ordinarily accepted use of the term it refers to taxes imposed by or for the benefit of a local authority or local area as distinct from taxes which form part of the revenues of a Provincial Government. Since the land in question is in Kalat State local taxes of this type would be imposed not by a British Indian Government but by the Kalat authorities, and the powers of the State in this matter are in fact specifically mentioned in clause 13 of the agreement (Exhibit A). I also venture to invite a reference to the decision of the Punjab High Court in the case of *Malik Sir Umar Hayat Khan*[1] where the assessee's contention that a water due payable by him could be regarded as a local rate was rejected and it was held that the water due was simply the price paid for the water supplied. I submit that this finding applies also to the water rate payable by the assessees.

10. For the above reasons I am respectfully of opinion that the answer to the first question should be that the profits accrued or arose or were received in British India for the purpose of Section 4 (1) of the Act, and that the answer to the second question should be in the negative."

Partabrai D. Punwani, for the Commissioner.

Srikrishindas H. Lulla, for the assessees.

JUDGMENT.

DAVIS, C. J.—We have before us a reference made at the request of the assessees by the Commissioner of Income-tax, Bombay, Sind and Baluchistan, in which the following two questions are set out for our opinion:

1. "Where a resident of British India who has business in British India takes a lease of agricultural land in an Indian State and brings the crop into British India where it is sold, does the profit arise in British India?

2. If the answer to the above question be in the affirmative, is the profit in the circumstances of the present case agricultural income in British India, within the meaning of Section 2 (1) (a) of the Indian Income-tax Act?"

We are of opinion that the first question must be answered in the affirmative, reading for the word "arise" the word "received" with consequential verbal amendments and the second question in the negative.

The reference of the learned Income-tax Commissioner is to be found at pages 47 to 52 of the paper-book and this reference of the learned Commissioner followed an order made by his predecessor dated June 28, 1939, finding that no question of law arose for reference to the Chief Court and declining in consequence to make a reference.

(1) (1925) 2 I.T.C. 52.

We think, however, that where a question arises as to the interpretation of clause (a) of sub-section (1) of Section 2 and as to the meaning of the words used, a question of law does arise, and we think that the agreement of both parties to refer the questions to us for our opinion was proper.

The facts of the case are that the assessees took the lease of certain lands in the Kalat State outside British India. The assessees are a firm consisting of three partners resident in British India and carry on a commission business at Shahdadkot in the Larkana District in the Province of Sind. They were lessees under an agreement entered into with His Highness the Khan of Kalat, in virtue of which they were to cultivate certain agricultural land in the Magsi Ilaqa of that State. They agreed to pay as consideration a sum of Rs. 51,000 annually. The revenue assessment and the water rate was to be paid by the lessor, the duty being cast upon the lessor to provide sufficient water for the cultivation of the leased land to the extent permitted by the authorities. On the other hand, did the lessees cultivate more land than was permissible by the rules in force from time to time, they would themselves be liable to pay all dues or fines imposed in respect of such excess cultivation. The lessees also produced before the Income-tax Officer a memorandum from the Wazir-i-Azam of the Kalat State to the Revenue Officer of Magsi Ilaqa Jhal, showing that one-tenth of the total demand due to the State was on account of the land revenue and nine-tenths was due to Government on account of water rate. The assessees brought the agricultural produce of the leased land in its raw unprocessed state to Shahdadkot in the Larkana District and sold it there and the sales effected during the relevant accounting period, namely, 1936-37, resulted in the net profits amounting to Rs. 84,714 for the assessment year 1937-38. The assessees were assessed on a total income of Rs. 90,000. They appealed against this assessment to the Assistant Commissioner of Income-tax, Sind, who confirmed the order passed by the Income-tax Officer. The assessees then requested that a reference be made to the High Court, which was the reference refused in the order of the Commissioner of Income-tax, Bombay, Sind and Baluchistan, dated June 28, 1939, followed by the agreed reference now before us.

It appears to us that no question of exemption of this Rs. 84,714 can arise, unless, in the first instance, it can be shown that the income for which exemption is claimed is agricultural income. Now, according to the definition of "agricultural income" in Section 2 (1) (a) the rent or revenue must be derived from land which is used for agricultural purposes and is either assessed to land revenue in British India or is subject to a local rate assessed and collected by officers of the Crown as such. It was argued before us by the learned Advocate for the assessees that this land, though outside British India in Kalat State, was land subject to a local

rate assessed and collected by officers of the Crown as such. But I do not see how land outside British India within the jurisdiction of His Highness the Khan of Kalat can be the subject of a local rate within the meaning of clause (a) of sub-section (1) of Section 2. I agree with the learned Income-tax Commissioner in his opinion that the land assessed to land revenue in British India or subject to a local rate must be land in British India. Further, it is plain to me that in this case the water rate, if it can be properly described as a local rate within the meaning of clause (a) of sub-section (1) of Section 2, which I do not think to be the case, is not collected, even if it be assessed, by officers of the Crown as such. Obviously the water rate is collected by His Highness the Khan of Kalat or rather by his officers. So that, it is not really necessary to answer the questions in this reference, to decide whether sums payable for the provision of water to land for purposes of cultivation can be deemed a local rate within the meaning of clause (a) of sub-section (1) of Section 2.

The learned Income-tax Commissioner referred to the case of *Malik Sir Umar Hayat Khan* v. *Commissioner of Income-tax, Punjab*[1], a decision of the Punjab High Court, where the assessee's contention that water dues payable by him should be regarded as a local rate was rejected and it was held that the water due was simply the price paid for the water supplied. The learned Advocate for the assessees in the case before us pointed out that in that case no land revenue was payable on the land and that there was no definite decision that "the water due" was not a "local rate" within the meaning of clause (a) of sub-section (1) of Section 2 or at least, that in certain cases, this could not be so. There is, I think, much to be said for the opinion that a local rate within the meaning of clause (a) is a rate imposed for the benefit of the local authority or local area as distinct from taxes forming part of the revenue of the Provincial Government. It would indeed, I think, be surprising to learn that the British Indian Government has the power to impose a local rate within the meaning of clause (a) on territories within the jurisdiction of His Highness the Khan of Kalat State. But, as I have said, I think, this case can be decided on a simple ground that no question of the exemption of this income can arise, because the income is not agricultural income; the land is outside British India and therefore, outside the scope of the beneficial provision of clause (a) of sub-section (1) of Section 2 of the Income-tax Act.

Nor, again, do I think, any question of the beneficial application of Section 4 can arise; if the income is not agricultural income, Section 4 (1) in full force applies. The income received in this case is income received in British India, I think, within the meaning of the Privy Council case in *Commissioner of Income-tax, Madras* v. *S. L. Mathias*[2].

(1) (1925) 2 I.T.C. 52. (2) [1939] 7 I.T.R. 48.

The question, then, as to whether anything depends upon whether agricultural produce is or is not subject to finishing processes before it is sold and the income is received, is not necessary for our decision. Nor is it, in view of the Privy Council case, necessary for us to consider the difference of opinion between the Calcutta and Madras High Courts in the cases reported as *Mohanpura Tea Company Ltd., In re*[1], and *Commissioner of Income-tax, Madras* v. *S. L. Mathias*[2], the Madras case being the subject of a decision of their Lordships of the Privy Council to which we have referred and by which obviously we are bound.

I have pointed out that when we answer the first question in the affirmative, it must be taken that we read this question as one, not as to whether the profit arises in British India, but whether the income is received in British India in the light of the judgment of the Privy Council in *Commissioner of Income-tax, Madras* v. *S. L. Mathias*[3]. In consequence of our finding that the income in this case is not agricultural income, the second question must be answered in the negative.

THADANI, J. (Concurring).—I agree and I have only a few words to add. The last proviso to Section 4 (2) of the Income-tax Act was intended to bring income from agriculture arising or accruing in a State in India from land for which any annual payment in money or in kind is made to the State on the same footing as agricultural income arising from land in British India, but with this exception that if income from agricultural land in a State in India was received in British India, as in this case, it became assessable to British Indian income-tax on the footing that it is not agricultural income as defined in Section 2 of the Indian Income-tax Act and exempt from the payment of income-tax.

Reference answered accordingly.

[IN THE ALLAHABAD HIGH COURT.]

RANI AMRIT KUNWAR

v.

COMMISSIONER OF INCOME TAX, C. P. & U. P.

IQBAL AHMAD, C. J., BRAUND and MALIK, JJ.

December 21, 1945.

INDIAN INCOME-TAX ACT (XI OF 1922), SEC. 4 (1), (2) AND (3) (vii)—INDIAN STATES—IMMUNITY OF RULING CHIEFS FROM TAXATION—REMITTANCE BY RULER TO WIFE RESIDING IN BRITISH INDIA—PAYMENTS BY RULER

(1) [1937] 5 I.T.R. 118; I.L.R. [1937] 2 Cal. 201.
(2) [1937] 5 I.T.R. 435.
(3) [1939] 7 I.T.R. 48.

TO SISTER RESIDING IN BRITISH INDIA—ASSESSABILITY—VOLUNTARY PAYMENTS—LIABILITY TO ASSESSMENT—ENGLISH AND INDIAN LAW—"INCOME", "CASUAL AND NON-RECURRING RECEIPTS", MEANINGS OF.

The assessee was the wife of the Ruler of the Kalsia State and the sister of the Maharaja of Nabha State. She was residing at Dehra Dun in British India for some years with her sons and daughters. In the assessment year she received a sum of Rs. 14,744 from the Kalsia State and Rs. 8,910 from the Nabha State. It was found that similar payments had been made to the assessee of varying amounts in each of the years she had lived at Dehra Dun and that they represented allocations for her benefit made in the relative State budgets. In the case of payments from the Kalsia State they were made for the purpose of meeting the assessee's household and living expenses and the education of her children, and in the case of the allowance from Nabha State it was made as an annual "wardrobe allowance" and as presents on certain days of festival each year. She was not bound to account for the moneys. Although the payments appeared in the State budgets as State expenditure there was no dividing line between that part of the income of the State which the Ruler spent for public purposes and that part which he spent for his private purposes:

Held, (i) *that the allowances received by the assessee from the Kalsia State were remittances from her husband and were taxable as income which must be deemed to have accrued to the assessee in British India under Section 4 (2) of the Indian Income-tax Act and the question whether the remittances received by her were casual and non-recurring did not arise;* (ii) *that as there was no evidence in the case to show that the payments made by the Nabha State were attributable to any custom, usage or traditional obligation and there was consequently no origin for the payments which could amount in its nature to a definite source so as to render each payment "income" and not merely a casual or annual windfall these payments were not "income" and were not assessable to income-tax;* Held, *further, that the assessee was not, by reason merely of her being the wife of a Ruling Chief exempt under the canons of international law from taxation under the Indian Income-tax Act in respect of whatever is, or is deemed to be, her income accruing, arising or received in British India.*

Under the Indian Income-tax Act, income in order to be taxable need not arise from any business activity, investment or an enforceable obligation to pay but may arise from voluntary or customary payments. Nor is it necessary that it should be the result of some outlay on the part of the assessee.

The words "non-recurring nature" in Section 4 (3) (vii) mean not that the payments have as a matter of fact not recurred but that they are not bound to recur.

Held, *per* BRAUND and MALIK, JJ.—*The Indian legislature has recognised that the Ruling Chief of an Indian State has the same immunity from taxation as any other foreign Sovereign but this immunity does not extend to his wife.*

Cases referred to :—

Aikin *v.* Macdonald's Trustees [1894] (3 Tax Cas. 306 ; 32 Sc. L.R. 85).

Beer Chunder *v.* Nobodeep Chunder Deb [1883] 9 Cal. 535.

Bishwanath Singh *v.* Commissioner of Income-tax, C.P. and U.P. [1942] (10 I.T.R. 322 ; A I.R 1942 All. 295 ; I.L.R. [1942] All. 398 ; 201 I.C. 209).

Commissioner of Income-tax, Bengal *v.* Shaw Wallace and Co. [1932] (A.I.R. 1932 P.C. 138 ; 59 Cal. 1343 ; 59 I.A. 206 ; 136 I.C. 742 ; 1932 A.L.J. 588 ; 5 I.T.C. 211).

Duff Development Co. Ltd. *v.* Government of Kalantan ([1924] A. C. 797 ; 93 L.J. Ch. 343 ; 131 L.T. 676).

Gopal Saran Narain Singh v. Commissioner of Income-tax [1935] (3 I.T.R. 237 ; A.I.R. 1935 P.C. 143 ; 14 Pat. 552 ; 62 I.A. 207 ; 156 I.C. 856).

Jwala Prasad *v.* Rana of Dholpur [1863] S. D.A. 579.

Kamakshya Narain Singh *v.* Commissioner of Income-tax, Bihar and Orissa [1943] (A.I.R. 1943 P C. 153 ; 22 Pat. 713 ; 70 I.A. 180 ; 210 I.C. 1 ; 11 I.T.R. 513).

Lachmi Narain *v.* Raja Partab Singh of Rampur [1880] 2 All. 1.

Ladkuverbai *v.* Ghoel Shri Sarangji Pratabsangji [1870] 7 Bom. H.C.R. 150.

Movstak Rae *v.* Lady Randheer Singh of Kapurthala State [1870] 54 P.R. 1870.

Phumanlal *v.* Raja Shamsher Parkash [1875] 93 P.R. 1875.

Rhodesia Metals Ltd. (Liquidators) *v.* Commissioner of Taxes ([1940] A.C. 774 ; 109 L.J. P.C. 81 ; 9 I.T.R. Suppl. 45).

Rochefoucauld *v.* Boustead ([1897] 1 Ch. 196 ; 66 L.J.Ch. 74 ; 75 L.T. 502 ; 45 W.R. 272).

Ryall *v.* Hoare ([1923] 2 K.B. 447 ; 92 L.J.K.B. 1010 ; 129 L.T. 505 ; 39 T.L.R. 475 ; 8 Tax Cas. 521).

Scoble *v.* Secretary of State for India ([1903] A.C. 299 ; 72 L.J.K.B. 617 ; 51 W.R. 675 ; 4 Tax Cas. 618).

Simpson *v.* Teignmouth and Shaldon Bridge Co. ([1903] 1 K.B. 405 ; 72 L.J.K.B. 204 ; 88 L.T. 117 ; 51 W.R. 545).

Sirdar Gurdyal Singh *v.* Raja of Faridkot [1894] A.C. 670.

Smelting Company of Australia Ltd. *v.* Commissioners of Inland Revenue ([1896] 2 Q.B. 179).

Statham *v.* Statham [1912] (L.R. 1912 P. 92 ; 81 L.J.P. 33 ; 105 L.T. 991).

Stedeford *v.* Beloe ([1932] A.C. 388 ; 101 L.J.K.B. 268 ; 146 L.T. 456 ; 48 T.L.R. 291 ; 16 Tax Cas. 505).

Tennant *v.* Smith ([1892] A.C. 150 ; 61 L.J.P.C. 11 ; 66 L.T. 327 ; 3 Tax Cas. 158).

Turner *v* Cuxon [1889] 22 Q.B.D. 150 ; 58 L.J.Q.B. 131 ; 60 L.T. 332 ; 37 W.R. 254 ; 2 Tax Cas. 422).

Reference under Section 66 (1) of the Indian Income-tax Act (XI of 1922) by the Income-tax Appellate Tribunal : (Miscellaneous Case No. 443 of 1943).

The material facts are set out in detail in the judgment.

Dr. N. P. Asthana, for the assessee.

G. S. Pathak, for the Commissioner.

JUDGMENT.

BRAUND, J.—This is a case referred to us under Section 66 (1) of the Income-tax Act, 1922, by a strong Bench of the Income-tax Appellate

Tribunal. The assessee is Rani Amrit Kunwar Sahiba, hereinafter referred to as "the Rani." The Rani is the wife of Raja Ravi Sher Singh Bahadur, the Ruler of Kalsia State, and is the sister of His Highness the present Maharaja of Nabha State. Kalsia and Nabha States were formerly part of what were known as the Cis-Sutlej States, which are now under the superintendence of the Agent to the Governor-General, Punjab States.

The Rani for some years past has lived at Dehra Dun in British India with her sons and daughters who are being educated there and it is common ground that in the year of assessment she was resident in British India within the meaning of Section 4A of the Income-tax Act, 1922. The relevant accounting year is 1938-39; and the relevant assessment year is 1939-40. In the assessment year, the Rani received at Dehra Dun a sum of Rs. 14,744 from Kalsia State and a sum of Rs. 8,910 from Nabha State. On the facts as they have been found by the Income-tax Tribunal it may be taken that similar payments had been made to the Rani of varying amounts in each of the years she had lived at Dehra Dun and that they represented allocations for her benefit made in the relative State budgets. In the case of the payments out of Kalsia State they were made for the purpose of meeting the Rani's household and living expenses and the education of the children at Dehra Dun; and, in the case of the allowance from Nabha State, it was made as an annual "wardrobe allowance" and as presents on certain specified days of festival in each year. Each payment, as I have said, was specifically budgeted for in the annual budget of each State and the evidence is that they had been made in each year consecutively for a period of almost twenty years. It is also common ground that the Rani has never been asked to give any account of her expenditure of these monies and that any surplus she may have had over at the end of the year has been tacitly assumed to be her personal property. Indeed, we are told that the Rani has been able to effect considerable savings during this period and has invested them in house property at Lahore, Dehra Dun and Mussoorie. These facts may be taken to be common ground, as also the fact that, although the payments made to the Rani appear in the relative budgets as items of State expenditure, there is no dividing line between that part of the income of the State which the Ruler spends on public purposes and that part which he spends for his own private purposes. In neither case is the Ruler himself resident in British India, nor is there any evidence that either Ruler is assessed on any income in British India.

In these circumstances, the Rani was assessed under Section 4 (1) (a) of the Income-tax Act, 1922, to income-tax by the Income-tax Officer of Dehra Dun in August 1939 on (*inter alia*) the two sums in question. This assessment was upheld by the Appellate Assistant Commissioner of Income-tax, Meerut, but was set aside in June, 1940, by the Commissioner of

Income-tax, Central and United Provinces, on the ground that there were insufficient findings of fact to support it. He accordingly directed the Income-tax Officer to start assessment proceedings afresh after reaching findings of fact, first, whether Kalsia State was an Indian State; secondly, whether the remittances received by the Rani were made out of the income of the State as such or out of the private income of its Ruler; and, thirdly, to what particular "vested right" the payments were respectively to be attributed. The Income-tax Officer in January, 1941, found that Kalsia State was an Indian State and that the remittances received by the Rani were out of State income and not out of the private income of the Ruler; but he was unable to reach any conclusion as to any "vested right" to which the payments were to be attributed. He apparently reached the same conclusion as regards the payments received from Nabha State. In the result he took the view that they were received by the assessee from the two States respectively as "her income in view of a vested customary right recognized by the State and its Ruler." He, therefore, again treated them as taxable and the Rani was again assessed on them as income from other sources under Section 4 (1) (a) of the Income-tax Act. This assessment was upheld by the Appellate Assistant Commissioner of Income-tax, Agra, and in due course came on appeal before a Full Bench of the Income-tax Appellate Tribunal.

The Full Bench consisted of four members—two of them judicial members, who have since been elevated to the Benches of the High Courts of Madras and the Punjab respectively. This Bench was divided in opinion, it being held by the President, first, that the Rani, notwithstanding that she was the wife of the Ruler of Kalsia State, was not exempt from assessment to income-tax in British India under the Income-tax Act, 1922, and, secondly, that the payments in question were not income of the assessee under Section 4 (1) of the Act; and that, if they had been, they would not have been assessable to tax because they were casual and non-recurring within the meaning of Section 4 (3) (vii) of the Act. On the other hand, the other learned judicial member of the Full Bench of the Tribunal, while agreeing that the Rani was not entitled to exemption from taxation on the ground that her husband was the Ruler of a sovereign State, took the view that the payments made to the assessee both from Kalsia State and from Nabha State in the accounting years did form part of the total income of the Rani for the purpose of assessment in British India. The two other members of the Tribunal agreed with the latter view and accordingly the assessment was once more upheld. It is in these circumstances that the matter now comes before us. The actual questions put to us by the Tribunal under Section 66 (1) of the Indian Income-tax Act are these:—

"(1) (a) Whether the allowances received by the assessee from the Kalsia State constitute her personal income assessable under the Indian

Income-tax Act? (b) If so, whether they are of a casual and non-recurring nature and as such exempt under Section 4 (3) (vii) of the Act?

(2) (a) Whether the moneys received by the assessee from the Nabha State constitute her personal income assessable under the Indian Income-tax Act? (b) If so, whether they are of a casual and non-recurring nature and as such exempt under Section 4 (3) (vii) of the Act?

(3) Whether, by reason of her being the wife of the Ruling Chief of Kalsia, the assessee, who is a resident in British India, is exempt under the canons of international law from taxation under the Indian Income-tax Act, in respect of her personal income accruing, arising or received in British India?"

Omitting question (3) for the moment, I think that the first two questions in reference to Kalsia State are susceptible of a short answer. The question reduced to its simplest term is whether the payment of the Rs. 14,744 in question received by the Rani in the accounting year at Dehra Dun from Kalsia State was in her hands "income. . . .from whatever source derived . . . received or deemed to be received in British India. . . ." within the meaning of Section 4 (1) (a) of the Indian Income-tax Act, 1922. If it did constitute, or is to be deemed to have constituted, her "income" then it was properly assessed, subject to any question which may arise under Section 4 (3) (vii) of the Act as to whether it was of a casual and non-recurring nature.

In my view, in the case of the payments which emanated from Kalsia State we are relieved by sub-section (2) of Section 4 of the Act from any inquiry whether these payments actually constituted the Rani's "income," because, when that sub-section is examined, it is found that, whether or not they were her income, they were, by virtue of their character as "remittances received by" her, "deemed" to be part of her income accruing in British India. Sub-section (2) of Section 4 of the Act is in this language:—

"(2) For the purposes of sub-section (1), where a husband is not resident in British India, remittances received by his wife resident in British India out of any part of his income which is not included in his total income shall be deemed to be income accruing in British India to the wife."

In the case before us the Rani's husband, the Raja of Kalsia, was admittedly not resident in British India. The Rani herself was at all material times resident in British India. The Rs. 14,744 received by her in the accounting year must, I think, be taken to have been paid to the Rani out of her husband's income, since it has not been and cannot be suggested that there is any distinction between the personal income of the Raja and the revenues of his State which are allocated under the annual State budget. There is no suggestion that the payments made to the Rani from Kalsia were paid out of any

income of the Raja which satisfies the definition of "total income" contained in the Act, nor, indeed, that the Raja had any income in British India at all. Up to this point, therefore, the conditions of sub-section (2) appear to be fulfilled exactly. But the noticeable point about sub-section (2) of Section 4 of the Act is that what it "deems to be income of the wife accruing in British India" are all "*remittances*" received by her out of her husband's income not included in his total income as defined by the Act. The word "remittances" is most noticeable. The word is not used anywhere else in the charging section and it stands in marked distinction to the word "income" which is elsewhere used to describe what is taxable. The only conclusion to be drawn from this is that sub-section (2) has been very careful, and, indeed, is designed for no other purpose than to make it clear that, where the wife residing in British India is found to be receiving money from her husband residing outside British India and that money has not already been taxed in British India, the actual "remittances" themselves are to be "deemed" to be the wife's income, irrespective of whether by any other test they would fulfil that definition. Sub-section (2) says that these "*remittances*" are to be "deemed to be income accruing in British India to the wife"; and, in my opinion, the object of this sub-section is, in view of the obvious difficulty in the way of the British Indian taxing authorities investigating the real character of such payments, to raise an absolute presumption against the wife that the "*remittances*" as such are themselves taxable under the head of what is deemed to be her income irrespective of its true character. On the other hand, in a case in which the remittances to the wife are shown to have been already included in the total income of the husband—and presumably already taxed or taxable as such—the Act has given the wife the benefit of the doubt and has at any rate provided no irrebuttable presumption that they are to be "deemed" to be her income.

I do not think that in either of the judgments of the learned judicial members of the Appellate Tribunal the full significance of the word "remittance" in sub-section (2) of Section 4 of the Indian Income-tax Act, 1922, in reference to the payments emanating from Kalsia State has been appreciated. If this view of the true construction of this sub-section is correct, then we are relieved from the necessity of considering whether, for other reasons and on other principles, the Rs. 14,744 in question was in income-tax law the Rani's actual income, since by the statute they are to be "deemed" to be her income. Nor in my view is it necessary for us to go so far as to decide whether the payments out of Kalsia State were casual and non-recurring. If the view taken above of the true construction of Section 4 (2) of the Act is the right one, then the remittances as such have to be "deemed" to be the income of the Rani irrespective of their actual

character either as income or as casual and non-recurring payments. In other words, Section 4 (3) (vii) of the Act cannot be regarded as having any reference to a "remittance" by a husband to a wife, which the Act itself has by Section 4 (2) expressly declared to be one which is to be "deemed" in any case to be income of the latter. I feel it right, however, to add that, but for Section 4 (2) of the Act, I should have felt the force of the conclusion reached by the learned President of the Tribunal expressed in para. 10 of his judgment that the payments in question *ex* Kalsia State have not in fact been shown ever to have become the moneys of the Rani (except perhaps as regards any unexpended balances) as distinct from monies which she was charged to expend as the agent of her husband on the maintenance and upkeep of his wife and children. But, since the payments in question were undoubtedly "remittances" by the Raja to the Rani, this does not arise, no question being involved, in view of Section 4 (2), whether they became her actual income or not. Being remittances to her, they must be "deemed" to be her income.

That, I think, is sufficient to dispose of the first part of the case, so far as it relates to the payments made to the Rani from Kalsia State in the accounting year. The question, however, of the payments made to the Rani from Nabha State is a different one, because no remittance to her from her husband is involved in that case. The source of the payment was the Maharaja of Nabha, who was the Rani's brother, and accordingly no question arises of applying Section 4 (2) of the Act. The question here involved seems to be simply whether the payments to the Rani in dispute were her "income" within the meaning of Section 4 (1) (a) of the Act. This question is a little more difficult. It is to be noticed that the Commissioner of Income-tax, Central and United Provinces, when he referred the matter back to the Income-tax Officer on 10th June, 1940, required him to find what was the particular "vested right" in the Rani's favour by virtue of which the allowance in dispute was paid. The Income-tax Officer in answer to this confessed that no evidence had been adduced before him to show in what right the Rani received the money, but nevertheless hazarded the conclusion that "moneys received by the assessee from . . . . Nabha State are her income in view of a vested customary right recognized by the State and its Ruler."

This finding appears to involve a little difficulty. It makes use of the expression "vested right," without, I think, realizing quite what it involves. If it means strictly what it says, it would appear to infer that the Rani had an indefeasible right to the annual allowance which she could enforce at law, assuming there to have been the machinery of law available in Nabha State to enable her to do so. If we were to take this finding literally, it would appear almost automatically to solve the question whether

the payments in question were the Rani's income or not. But I think the true view is, both because of the circumstance that the Income-tax Officer himself confessed that there was no evidence on which he was able to base his conclusion and because it would be in any case a question as much of law as of fact, that we cannot take it as concluded that the payments in question from Nabha State were payments to which the Rani had an indefeasible and enforceable right. Both the learned judicial members of the Income-tax Appellate Full Bench appear to have taken the same view because the major parts of their respective judgments were devoted to discussing the very question whether the circumstances in which the payments were made justified the conclusion that they were traceable to some sort of enforceable obligation—I should desire to avoid the use of the expression "vested right"—which would clothe them with the character of "income" in the hands of the Rani in British India. That undoubtedly is the substance of the question which we are called on to decide on this reference and there is little doubt that it is a question of law and is not concluded by the finding of the Income-tax Officer to which I have referred above. The question, therefore, is whether the payment of Rs. 8,910 made *ex* Nabha State to the Rani in the accounting year was the Rani's "income." Section 4 (1) of the Indian Income-tax Act, 1922, charges in the hands of the assessee "all income, profits and gains from whatever source" received by the assessee in British India in the relevant year. There can be no suggestion in this case that the payments in question come within any of the first four heads of income chargeable to income-tax set out in Section 6 of the Act, and, therefore, the only question involved is whether they constitute "income from other sources." The facts, as provided for us, are that the sum in question was received by the Rani at Dehra Dun by cheque from Nabha State by equal quarterly payments of Rs. 2,227-8-0 credited to the assessee's bank account in British India (see the assessment order dated 26th August, 1939); these payments were received over "a long course of years" (see the Statement of the Case); they were paid "out of the State budget" (see the assessment order dated 25th January, 1941); the allowance from Nabha State was a "wardrobe allowance" which was in the nature of a present of clothes and money presents at specified festivals, namely *Tejan* and *Karwa* (see the judgment of the President of the Income-tax Appellate Tribunal); the Rani was not asked to account in any way for her expenditure of the moneys in question and any surplus remaining over at the end of the year became her absolute property (see para. 10 of the judgment of Mr. Yahya Ali, as he then was, of the Income-tax Appellate Tribunal); and a certificate was furnished by the Prime Minister of Nabha State to the effect that the payments had been made continuously by the Nabha State Durbar to the

Rani since prior to 1926, at first at the rate of Rs. 358 a year and later at the present rate of Rs. 910 (see para. 8, *ibid*). These, I think, are the relevant facts on which we have to consider this question.

The first step is to see what is meant by the word "income" as used in Section 4 (1) of the Indian Income-tax Act, 1922. In using for this purpose English authorities on the construction of the Indian Income-tax Act, it is constantly necessary, I think, to remind oneself that the charging words of the English Income Tax Act are not the same as the charging words of the Indian Income-tax Act. The English Income Tax Act of 1918 by Section 1 charges to tax "all property, profits or gains" described or comprised in the schedules referred to in it. Schedule A is the schedule which charges tax on property. Schedule B is the schedule which charges tax on the occupation of land. Schedule C is the schedule which charges tax on interest, annuities and dividends. Schedule D is the schedule which charges tax on "annual profits or gains" arising from any trade, profession, employment or vocation. And Schedule E is the schedule which charges tax in respect of public offices or employments of profits, annuities, pensions, etc. The Indian Income-tax Act, on the other hand, by Section 4 (1), charges generally to tax "all income, profits and gains from whatever source derived." It is clear, therefore, that the Indian Income-tax Act in employing the expression "income" not only lays open to the charge of tax everything that can be properly brought within the description of "income" (irrespective of any technical categories of income such as are contained in the schedules to the English Act), but also treats the expression "income" as something which is larger and more general than "profits and gains." Their Lordships of the Privy Council pointed out in *Gopal Saran Narain Singh* v. *Commissioner of Income-tax*[1] that the word "income" is not limited by the words "profits and gains" and that "anything which can properly be described as income is taxable under the Act, unless expressly exempted." The starting point, therefore, in my view, of any inquiry as to what is taxable under the Indian Act, must be that the word "income" as used in Section 4 (1) of the Indian Income-tax Act, 1922, not only may denote something larger than profits and gains, but may denote whatever may properly be described as "income" in the ordinary parlance of language, unless expressly exempted from the charge of tax by the Act itself. I draw attention to this because we have been pressed to decide this case by reference to English authorities decided on the English Income Tax Act to the effect that payments made to a person which are ultimately dependent solely on the will of the giver and are not attributable to any right to receive on the part of the recipient can *ex hypothesi* never be

(1) [1935] 3 I.T.R. 237, at p. 242.

income in the income-tax sense so as to bring them within the charge of tax under the Indian Income-tax Act. Indeed, the learned counsel who has appeared for the assessee in this case has on the strength of the English authorities gone so far as to say, if we have understood him rightly, that nothing can be taxable as income from other sources under the Indian Act, which cannot be shown to have an origin in some enforceable obligation to pay. We have been referred for this proposition to *Stedeford* v. *Beloe*[1], *Ryall* v. *Hoare*[2] and *Turner* v. *Cuxon*[3]. In my view the short answer to be given to this line of reasoning is that it is wholly misleading to apply authorities decided under the English Act to the question what is " income " under the Indian Act in such circumstances as we have to deal with here. To take the case in *Stedeford* v. *Beloe*[1] in the House of Lords referred to above, an annual pension had been granted to a headmaster of Bradfield College on his retirement and it was held that such a pension was not chargeable to income-tax under Schedule E of the English Income Tax Act. The question, therefore, was whether the pension in question was such a profit or gain as arose or accrued to the retired headmaster from an office, employment or pension. It was held that it was not, because something which was merely voluntary could never be a profit or gain derived from an employment. But Viscount Dunedin in the course of his speech said:—

" ...it has been held again and again that a mere voluntary gift is not such a profit because it is not, in the true sense of the word, income. It is merely a casual payment which depends upon somebody else's goodwill."

It is true that the learned Law Lord there describes a mere voluntary gift as not being in the true sense of the word income; but it has to be remembered that he was speaking in reference to the English Income Tax Act and not in reference to the Indian Income-tax Act. In short, the English Income Tax Act by its charging provisions has taxed only those particular types of income which can be brought within the various schedules, whereas the Indian Income-tax Act has charged whatever is "income, profits and gains " on the proper construction of those expressions. It would, in my view, be going altogether too far, on the strength of those words of Viscount Dunedin in the *Bradfield College case*[1] taken out of their context, to say that nothing whatever can be charged as income under the Indian Income-tax Act which has not an origin in some obligation to pay. I believe that the true test to be applied under the Indian Income-tax Act is that which has been prescribed by Lord Russell of Killowen in *Gopal Saran Narain Singh* v. *Commissioner of Income-tax*[4], in which he says that anything which can properly

(1) [1932] A.C. 388.
(2) [1923] 2 K.B. 447.
(3) (1889) 22 Q.B.D. 150.
(4) [1935] 3. I.T.R. 237, at p. 242.

be described as income is taxable under the Indian Income-tax Act, unless expressly exempted. I regard it as dangerous to take a sentence from a judgment even of the House of Lords decided under the English Act and to seek to found on it wide assertions as to the true construction of the Indian Act.

We have next been pressed on the authority of *Commissioner of Income-tax, Bengal* v. *Shaw Wallace & Co.*[1] with a rather different variation of the same argument. On the strength of what has been said by Sir George Lowndes in that case, the argument has been converted into the suggestion that, even though it may not be necessary that the origin of the receipt by the recipient should lie in some obligation to pay, nevertheless the "source" from which it is received must be one which connotes a "return" in a sense *ejusdem generis* with the profits and gains which are the return either of business activity or investment. Sir George Lowndes, afterwards himself pointing out the danger of relying on the case law evolved out of the English Income Tax statutes when construing the Indian Act, went on to point out that the object of the Indian Act was to tax "income," although it has not defined what it means by that word. He said :—

"The object of the Indian Act is to tax 'income' a term which it does not define. It is expanded, no doubt, into 'income, profits and gains', but the expansion is more a matter of words than of substance. Income, their Lordships think, in this Act connotes a periodical monetary return 'coming in' with some sort of regularity, or expected regularity, from definite sources. The source is not necessarily one which is expected to be continuously productive, but it must be one whose object is the production of a definite return, excluding anything in the nature of a mere windfall. Thus income has been likened pictorially to the fruit of a tree or the crop of a field. It is essentially the produce of something, which is often loosely spoken of as 'capital' . . . ."

It is this passage on which the assessee relies in this case for the purpose of saying that a payment the continuation of which can be interrupted by the giver can never be that sort of "periodical monetary return" coming in from a definite source which is contemplated as being taxable by the Indian Income-tax Act. It has to be remembered that, although Sir George Lowndes' words are general, the actual case with which he was dealing was one in which it was sought to tax a payment made to the assessee as compensation for the loss of a valuable business agency, and, in that sense, the actual matter before the Board was clearly something which had relation to the business of the assessee. No actual question of the sort we are dealing with was involved. In my opinion, however, Sir George Lowndes never intended to—and, in

(1) (1932) 59 Cal. 1343; 1932 A.L.J. 588.

fact, by the language he used, never did—limit the construction of the word "income" in the Indian Income-tax Act to something which must necessarily have its origin either in a business activity, an investment or an enforceable obligation. Indeed, the passage, when examined, bears no such meaning. He says that, in order to be income, it must be something which "comes in" (1) periodically, (2) as a return, (3) with some sort of regularity or expected regularity and (4) from a definite source. It appears to me to be beyond argument that a series of payments may be made periodically and with regularity or with expected regularity, notwithstanding that they do not have their origin in business activity, investment or enforceable obligation. That such a payment is something which "comes in" and in that sense may in the proper circumstance be "income" in the wide sense in which that expression was explained by Lord Macnaghten in *Tennant* v. *Smith* [1], is, I think, equally beyond doubt. And I should add as a third self-evident proposition that there may be a great deal of practical difference between a payment which is one of a series of payments made with regularity or expected regularity on the one hand and what Viscount Dunedin describes in the *Bradfield College case* [2] as "merely a casual payment" and what Sir George Lowndes describes in *Commissioner of Income-tax, Bengal* v. *Shaw Wallace & Co.* [3], as "a mere windfall." The principal emphasis, however, is laid on the words "return" and "definite sources" used by Sir George Lowndes. But these in my view present no difficulty. A regular payment or a payment expected to be regular may, I think, in principle be as much "income" when it is received from a giver who makes it systematically and for a known and rational reason (and *a fortiori* when it is received in accordance with custom), as it is if it is made in pursuance of some binding obligation whether arising out of business dealings, out of an investment or out of some other enforceable obligation. And if the word "return" had been used by Sir George Lowndes in the strict sense that nothing could be income in India which was not the result of some outlay, it would be difficult to see how anything could be taxable which was not the produce of some valuable consideration given by the recipient however binding might be the actual obligation under which it was paid. For these reasons in my view it cannot be taken that Sir George Lowndes intended to lay down a general test in every case that every payment must be the result of some outlay on the part of the assessee before it is taxable.

Under Indian law, therefore, we come back in my opinion, to the relatively simple test whether in the ordinary parlance of language what the assessee receives is "income" or not. I should not dream of suggesting that every payment made by one person to another is necessarily the

(1) [1892] A. C. 150, at p. 164.
(2) [1932] A.C. 388.
(3) (1932) 59 Cal. 1343; 1932 A.L.J. 588.

recipient's income since it may, as Viscount Dunedin has said, be merely a casual payment or, as Sir George Lowndes has suggested, a mere windfall. Such a sweeping proposition would be absurd. Many things have to be considered. In the case of a payment by a parent to a child or by a husband to a wife or by one relation to another obvious questions arise whether in the particular circumstances of each case the payments are made in such a way as to constitute what is paid the money of the recipient at all or whether the payments themselves are not merely a series of casual payments or windfalls. But there seems to me to be another class of cases altogether in which in particular circumstances payments may be made by one person to another which can only be explained on the ground that the giver intends to give, and the recipient expects to receive, with regularity or expected regularity and from a source the nature of which is to produce such a payment, an "income" which is in the income-tax sense his own. I can find nothing in the Indian Income-tax Act to warrant any general conclusion that it is only in a case in which, if the payment is discontinued, the recipient will have an immediate right of action against the payer, that it will be income in his hands in the Indian income-tax sense. That is to put too limited a construction on the word "income." If the payments are such as to come within the category of payments which are casual and non-recurring, then it is to be observed that the Act itself has taken them out of the category of "income." The very fact that the framers of the Indian Income-tax Act found it necessary by a special clause to exempt casual and non-recurring receipts from the category of income, profits or gains is itself, in my opinion, an indication that, but for that exemption, they are to be regarded as capable of falling within the class of income, profits or gains under the charging section. If it is to be assumed that *ex hypothesi* a casual and non-recurring payment could never be income, then, as I see it, the statutory exception of it would be otiose and unnecessary. Another reason is afforded by Section 4 (3) (ii) of the Income-tax Act for inducing me to think that so narrow a construction cannot be placed on the word "income." If the assessee were right in saying that the test of "obligation" has in all cases to be applied in deciding what is or is not "income," it is difficult to see why voluntary contributions to a religious or charitable institution (whether applicable solely to religious or charitable purposes or not) should be specially excepted by the Act. The conclusion, therefore, I have reached is that, in construing the word "income" in the Indian Income-tax Act, one has to ask oneself whether, having regard to all the circumstances surrounding the particular payments and receipts in question, what is received is of the character of income according to the ordinary meaning of that word in the English language or whether it is merely a casual receipt or mere windfall.

I have dealt generally so far with the meaning of the word "income" in Section 4 (1) of the Income-tax Act, 1922, since I have found it impossible to accept so large and general a proposition that nothing can in India be the "income" of a recipient of money which cannot be traced to one of the first four sources set out in Section 6 or to some other source involving either the product of some outlay by, or some binding and irrevocable obligation to pay to, the recipient. It remains then to consider the actual facts of the payments in this case to the Rani from Nabha State for the purpose of seeing on which side of the line they fall and whether they ought to be regarded as her "income" or as something in the nature of mere recurring windfalls.

There can be no doubt that the payments have recurred with both actual and expected regularity for the better part of twenty years. Only once have they been varied in amount and they have been paid quarterly. The sanction for their payment has appeared in the annual budget of the State. I think, therefore, that they have become "customary" payments in the limited sense at least that they were "habitual" payments though I am inclined to agree with respect with the learned President of the Tribunal that no fact has been proved to warrant any finding that they are "customary" payments in the legal significance of that term denoting something that has become legally enforceable by custom. Nor do I think that there is the slightest evidence, as the Income-tax Officer has himself admitted, of any "vested right" in the Rani to receive the annual sum in question from Nabha State. I think that the use of the expression "vested right" has been a little unfortunate and misleading. What we really have, therefore, is a series of payments made over a period long enough to entitle them to be described as habitual, originating, so far as any evidence in this case goes, in nothing more than the bounty of the Ruler of Nabha State. We must at this stage accept the facts as they are given us. It may be that had further researches been possible, some more certain sanction for these payments might have been found than the mere annual bounty of the Ruler. But, if it exists it was for the Income-tax authorities to show it, since we cannot tax on facts which are not proved. I should be loath to say that there might not be special circumstances in which payments of this kind though voluntary in the sense that if discontinued, there is no remedy might be attributable to some custom, usage or traditional obligation which might invest them with the character of "income" in the hands of the recipient. But, if there are, then it is, I think, for the Income-tax authorities to show it. In the present case nothing of the sort has been shown beyond the regularity or expected regularity of the payments born of repetition. The case is a difficult one and may stand on the border line of what is income and what is not income. But, on the facts provided, I am persuaded

that the Income-tax authorities have not discharged the burden of showing (apart from the mere circumstance of repetition) that there is any origin to account for these payments which could amount *in its nature* to a definite source so as to render each payment "income" and not merely "casual or a mere annual (though expected) windfall." I do not reach this conclusion, as I have explained, on the ground simply that they are voluntary in the sense that they might be discontinued without the Rani having any enforceable remedy; but on the ground that it has not been proved in this particular case that there is anything more certain than the mere whim of the Ruler to support them. For these reasons, in my opinion, the first two questions put to us should [subject to any answer we may give to question (3)] be answered thus: (1) The allowances received by the assessee from the Kalsia State during the accounting year should be deemed to be her income accruing in British India. No question arises in this case whether they are of a casual and non-recurring nature; (2) The moneys received by the assessee from the Nabha State during the accounting year do not constitute her personal income assessable under the Indian Income-tax Act. There then remains the third of the questions put to us:—

"Whether by reason of her being the wife of the Ruling Chief of Kalsia, the assessee, who is a resident in British India, is exempt under the canons of international law from taxation under the Indian Income-tax Act in respect of her personal income accruing, arising or received in British India?"

On this question all the members of the Income-tax Tribunal were agreed upon an answer in the negative. In this conclusion I concur. The learned President of the Tribunal was of the opinion, on the authority of *Bishwanath Singh* v. *Commissioner of Income-tax, Central and United Provinces*[1], that the Ruler of Kalsia State was not sovereign for the purposes of international law and consequently could claim immunity in British India neither from taxation under the British Indian taxing Act nor from proceedings in respect thereof in British Indian Courts. The other learned judicial member of the Tribunal came to the same conclusion on the ground that no Indian State was sovereign in the sense in which that word was used in public international law and that the Ruler of an Indian State did not possess any vestige of "international" personality. That the Ruler of Kalsia State is a Ruling Chief and enjoys internal sovereignty over his subjects within his State, except in certain specified respects, is admitted by Dr. Asthana, who appears in this case on behalf of the Income-tax authorities. The State came under the protection of the British Crown in or prior to the year 1809 when it was protected by Proclamation against further encroachments. The British Crown imposed on it certain restrictions

(1) [1942] 10 I.T.R. 322.

in respect of exercising jurisdiction over Europeans and Americans within its territory, of regulating the succession to the State, or correcting misrule and of regulating the strength of its armed forces. But in other respects it appears that its internal or domestic sovereignty over its own subjects remained unimpaired. Mr. Pathak, as he then was, has urged with considerable force that an Indian State, having originally internal sovereignty, continues to enjoy all those rights of sovereignty as between it and the British Crown which it is not shown to have parted with or been deprived of by agreement, treaty or superior power and it is only to that extent that the sovereignty of Kalsia State can be held to have been diminished by its contact with the British Crown. Moreover, one of the outstanding attributes of sovereignty is the Ruler's immunity from being sued in a foreign Court (*see* Oppenheim's International Law, edition 5, volume I, page 590). In *Duff Development Co., Ltd.* v. *Government of Kelantan*[1], Viscount Finlay said that, though it was obvious that in order to have sovereignty there must be a certain amount of independence, it was not in the least necessary for sovereignty that there should be complete independence. He said :—

"......It is quite consistent with sovereignty that the sovereign may in certain respects be dependent upon another Power; the control, for instance, of foreign affairs may be completely in the hands of a protecting Power, and there may be agreements or treaties which limit the powers of the sovereign even in international affairs without entailing a loss of the position of a sovereign Power. In the present case it is obvious that the Sultan of Kelantan is to a great extent in the hands of His Majesty's Government......"

It is also clear from the *Duff Development Company case* [1] in the House of Lords that British Courts have always adopted the practice of relying on a statement made by His Majesty's Government as to the Crown's relations in respect of sovereignty with a foreign Ruler and that in the face of any such statement British Courts will not in their judicial capacity inquire into and decide whether any restrictions submitted to by any such foreign Ruler are or are not such that the Ruler has ceased to be sovereign. We could have wished that the same course had been followed in the present case before us by the Income-tax authorities. This was what was done in the case relating to Benares State referred to above: *Bishwanath Singh* v. *Commissioner of Income-tax, Central and United Provinces*[2]. It would, I think, have been proper to obtain from the Crown Representative a certificate or statement in relation to the status in respect of the sovereignty of the Ruler of Kalsia State. But this has not been done in this case and, if by this omission the Income-tax authorities have in any way been prejudiced,

(1) [1924] A. C. 797. (2) [1942] 10 I.T.R. 322.

they have themselves alone to blame for it. I should not myself feel disposed to direct a reference to be made to the Crown Representative at this late stage, in view of the conclusion at which I have arrived.

In my opinion, the only view which on the evidence before us, we can properly take in this case is that the Ruler of Kalsia State has, notwithstanding the protection of the British Crown, continued to enjoy a full measure of internal and domestic sovereignty except to the particular extent to which it has been admitted that the British Crown has imposed and exercised rights restrictive of it. Those rights do not include any derogation from the accepted immunity of an otherwise sovereign Ruler from being sued in the Courts of a foreign power. And I cannot help thinking that the test of whether the Ruler of an Indian State can be made the subject of taxation in British India under a British Indian taxing Act must ultimately rest on whether he is capable of being sued in British Indian Courts, since it cannot be contemplated that any British Indian Legislature would pass legislation against a foreign Ruler or against anyone else which the Courts in British India have no power to enforce. Moreover, there is considerable authority to the effect that a Ruling Prince is not normally capable of being sued in a British Indian Court or in a Court in England. In *Statham* v. *Statham*[1] it was held in reference to the State of Baroda that its Ruling Prince was not capable of being made a co-respondent in a suit for divorce in the High Court in England. In that case Sir Henry Bargrave Deane, J., said that "suzerainty" was a term applied to certain international relations between two sovereign States whereby one, whilst retaining a more or less limited sovereignty, acknowledged the supremacy of the other; and, in his opinion, that aptly expressed the true status of the Gaekwar of Baroda and *was consistent with the status of a sovereign prince*, who was not capable of being sued in Courts of the suzerain power. There are other authorities in India to the same effect which have been referred to in the judgment of the learned President of the Tribunal. In the result, therefore, in my opinion the better view is that, on the facts, before us, it must be held that nothing has been shown which deprives the Ruler of Kalsia State of his position as a sovereign Ruler and, therefore, of his personal immunity from proceedings in British Indian Courts. And from this it seems to me to follow that he must necessarily be immune from taxation in British India under an Act, which no Court in British India has the power to enforce against him.

But I am at the same time respectfully inclined to agree with the learned member of the Tribunal who observed that sovereignty in this sense may well be something less than the retention—if, indeed, he ever had it—of an international personality in public international law in the fullest

(1) (1912) L. R. 1912 P. 92 : 105 L.T. 991.

sense. No case, with one possible exception, has been brought to our notice in which there has ever been put forward successfully a claim on behalf of the Ruler of an Indian State to recognition of sovereignty in the full sense in which that word is used in public international law so as to extend the privilege of personal immunity from proceedings in Courts of British India to the Ruler's wife. The only possible exception is the case relating to Kapurthala State which is reported in *Movstak Rae* v. *Lady Randheer Singh of Kapurthala State*[1]. But, in my opinion, that case when examined is no authority for so general a proposition that the personal immunity founded on his domestic sovereignty of a Ruler of an Indian State from suits in Courts in British India extends by international usage to his wife. What the Court in British India said in that case was that it would not assume jurisdiction in British India in a suit which arose between the Maharaja and his subjects within his own State. It was held that a British Indian Court would not adjudicate in British India on rights in issue within his own State between the wife of a politically independent Raja and a subject of that State; in other words, that a British Indian Court would not examine and adjudicate on the position of the Maharaja's consort within the Maharaja's own State with reference to an issue arising within the State itself. That is a very different thing from saying that every British Indian Court will extend to the wife of every Ruler of an Indian State recognition of her husband's sovereignty in the full sense of an international personality as recognized by public international law in relation to a proceeding in which the rights in issue do not arise within the State itself but within British India. We have been referred to no authority which would, in my opinion, justify us in extending the incidents of the domestic sovereignty of the Ruler of Kalsia State to this extent. For these reasons, whether or not the Ruler enjoys a personal immunity, I should respectfully agree with the conclusion at which the Income-tax Appellate Tribunal has arrived that, such immunity, if it exists, does not extend to the Rani in this case. The answer to the third question propounded to us should, in my opinion, therefore, be: The assessee, by reason of her being the wife of the Ruling Chief of Kalsia, is not exempt under the canons of international law from taxation under the Indian Income-tax Act in respect of whatever is, or is deemed to be, her income accruing, arising or received in British India.

MALIK, J.—This is a reference under Section 66 (1) of the Indian Income-tax Act by the Income-tax Appellate Tribunal. The assessee, Rani Amrit Kunwar, is the wife of the Raja of Kalsia State. She has been living in Dehra Dun for some years and owns house property in Dehra Dun, Mussoorie and Lahore. The Income-tax Department assessed her to income-tax for the assessment years 1939-40 and 1940-41 on the basis of her income

(1) (1870) 54 P.R. 1870, p. 139.

in the years 1938-39 and 1939-40. During the accounting year 1938-39 the assessee received a sum of Rs. 14,744 from the Kalsia State and a sum of Rs. 8,910 from the Nabha State. In the next year, 1939-40, the assessee received from the Kalsia State Rs. 8,000 and from the Nabha State Rs. 8,910. The Income-tax Department included these sums in the total income of the assessee and assessed her accordingly. The assessee raised certain objections, but it appears that the objections raised by her before the Income-tax Officer were not the same as the objections that she ultimately raised before the Appellate Tribunal. No useful purpose would be served by making any reference to the objections raised by her earlier in the proceedings till we come to the proceedings before the Income-tax Appellate Tribunal. Before the Tribunal two objections were raised, firstly, that the sums received by the assessee from Kalsia and Nabha were not assessable income as they were purely voluntary gifts made to the assessee and were, therefore, of a casual and non-recurring nature. The second objection raised was that the assessee being the wife of the Raja of Kalsia, who was an independent sovereign, was not liable to pay any income-tax in British India. The matter was considered by a Full Bench of the Tribunal. The President of the Tribunal, Mr. M. Munir, held on both points in favour of the assessee and was of the opinion that she was not liable to to pay income-tax on these sums. Mr. Yahya Ali, judicial member, was on both the points against the assessee. The two other members of the Bench agreed with Mr. Yahya Ali and it was held by the majority that the assessee was liable to pay income-tax on the sums mentioned above.

The assessee then applied to the Tribunal that eight questions be referred to this Court under Section 66 (1) of the Indian Income-tax Act. The Tribunal, however, reframed the questions and referred to us the following questions for our decision :—

"1. (a) Whether the allowances received by the assessee from the Kalsia State constitute her personal income assessable under the Indian Income-tax Act?

(b) If so, whether they are of a casual and non-recurring nature and as such exempt under Section 4 (3) (vii) of the Act?

2. (a) Whether the moneys received by the assessee from the Nabha State constitute her personal income assessable under the Indian Income-tax Act?

(b) If so, whether they are of a casual and non-recurring nature and as such exempt under Section 4 (3) (vii) of the Act? and

3. Whether, by reason of her being the wife of the Ruling Chief of Kalsia, the assessee, who is a resident in British India, is exempt under the canons of international law from taxation under the Indian Income-tax Act, in respect of her personal income accruing, arising or received in British India?"

My answer to the questions enumerated above, for reasons given by me later, are as follows :—

1. (a) Yes; (b) No;
2. (a) No; (b) Yes; and
3. No.

The provisions of the Indian Income-tax Act are so complex and are so hedged in by various provisos, exceptions and explanations that it is difficult to generalise about any matter. It may, however, be said, bearing in mind that it is a bare generalisation and is subject to various exceptions, that income, profits and gains are divided for the purposes of ascertaining the liability of an assessee, who is "resident in British India," who is "ordinarily resident in British India" or who is "not resident in British India," into three heads according to the place where it has accrued or arisen, namely, (1) income, profits and gains which have accrued or arisen or are deemed to have accrued or arisen in British India, (2) income, profits and gains which have accrued or arisen outside British India but have been received in British India or are deemed to have been received in British India, and (3) income, profits and gains which have accrued or arisen outside British India. Whether an assessee is "resident in British India" or is "not resident in British India" or is "not ordinarily resident in British India," he is liable to have his income under the first two heads mentioned above included in his total income for the purpose of assessment, unless such income or any portion thereof is specially exempted. Section 4, sub-section (1), sets out what income is to be included in the total income of an assessee if he is "resident" and if he is "not resident" and if he is "not ordinarily resident" in British India. This is followed by a number of provisos and explanations which deal mostly with income that has accrued outside British India and are not necessary for our purposes.

If an assessee (that is, a person liable to pay income-tax in British India) makes a voluntary allowance to any person out of the assets which remain his property, he is not entitled to deduct such sums from his total income. Section 16 (1) (c) provides that all income arising to any person by virtue of a settlement or disposition whether revocable or not, and whether effected before or after the commencement of the Indian Income-tax (Amendment) Act, 1939, from assets remaining the property of the settlor or disponer, shall be deemed to be income of the settlor or disponer, and all income arising to any person by virtue of a revocable transfer of assets shall be deemed to be income of the transferor. This again is followed by a number of provisos which are not relevant for our purpose, but bearing in mind the fact that the principle against double taxation is accepted by the Indian Income-tax Act it is evident that such sums, when they are included in the income of the settlor, transferor, or disponer, cannot be taxed in the

hands of the transferee as they are already taxed in the hands of the transferor. In the case of a wife and a minor son, even if the assets are transferred to the wife otherwise than for adequate consideration or in connection with an agreement to live apart, income from such assets is included in the total income of the assessee, see Section 16 (3). Whatever may be the reason for the rule and apart from the question of the amount not being taxable twice over, both in the hands of the transferor and the transferee, it appears to me that it is difficult to bring a voluntary allowance made by a husband to his wife or by a father to his son under any of the five heads of taxable income enumerated in Section 6 of the Indian Income-tax Act. It is clear that it cannot come under the first four heads of income, profits and gains mentioned in Section 6; the only head under which it may be brought is "income from other sources," *i.e.*, the last head.

Section 12 of the Act deals with this last head of "income from other sources." The case for the Department is that the allowances given by the Raja of Kalsia to his wife fall under this last head, that is, "income from other sources." Section 4 (1) read with Section 12 of the Act makes it clear that the words "from whatever source derived" in Section 4 (1) and the words "if not included under any of the preceding heads" in Section 12 were intended to extend the net as widely as possible so as to catch all possible sources of income. It must, however, be borne in mind that Section 6 of the Act does not say "any other income" but it is "income from other sources" and there must, therefore, be a "source" from which the income is derived before it can fall under the fifth head enumerated in Section 6. In the case of a voluntary allowance paid by the husband to the wife it will be difficult to class the husband as the source of the income. Their Lordships of the Judicial Committee have quoted with approval from Ingram on Income-tax that "'source' means not a legal concept but something which a practical man would regard as a real source of income": see *Rhodesia Metals Ltd.* (*Liquidators*) v. *Commissioner of Taxes*[1]. If, however, the husband is bound to pay a certain sum periodically under an order of a Court or under an agreement, the order or the agreement may be deemed to be the source of the income. Their Lordships of the Judicial Committee in *Kamakshya Narain Singh* v. *Commissioner of Income-tax, Bihar and Orissa*[2] held that the agreement to pay the royalty by the lessee of a coal mine was the "source" of the income. Ordinarily, therefore, if a person makes a voluntary allowance to his wife or his children, he is not entitled to get a deduction for such payment and the money in the hands of his wife or children would not be deemed to be their income. It has been held in England that the word "income" must be construed in the popular sense of the word: see *Simpson* v. *Teignmouth and Shaldon*

(1) [1941] 9 I.T.R. (Suppl.) 45; [1940] A.C. 774.
(2) [1943] 11 I.T.R. 513; 1943 A.L.J. 493.

Bridge Co.[1] and *Aikin* v. *Macdonald's Trustees*[2]. In *Smelting Co. of Australia Ltd.* v. *Commissioners of Inland Revenue*[3], (*sic*) it was held that the popular sense of the word "income" connotes a periodical and recurrent receipt arising out of personal exertion or investments in property, securities or business (including activities in the nature of trade). The dictionary meaning of the term "income" is as follows:—

"That which comes in as the periodical produce of one's work, business, lands or investments (considered in reference to its amount and commonly expressed in terms of money)" or "annual or periodical receipts accruing to a person or corporation." (See Oxford Dictionary.)

It is defined in the Oxford Concise Dictionary as: "Periodical receipts from one's business, lands, work, investments, etc., (income-tax levied on this)." In the Webster Dictionary it is defined as:

"That gain or recurrent benefit (usually measured in money) which proceeds from labour, business or property; commercial revenue or receipts of any kind, including wages or salaries, the proceeds of agriculture or commerce, the rent of houses or return on investments."

Learned counsel for the assessee has drawn our attention to the decision of their Lordships of the Judicial Committee in *Commissioner of Income-tax, Bengal* v. *Shaw Wallace & Co.*[4], and has argued that their Lordships have held that the words "income, profits and gains" are more a matter of words than of substance and really mean the same thing. That may be so, but then in ordinary English it is more appropriate to call certain kinds of receipts as profits or gains and certain other kinds as income, for example, the fees paid to a Barrister could hardly appropriately be called profits or gains, the more appropriate term for the purpose would be "income." In *Gopal Saran Narain Singh* v. *Commissioner of Income-tax*[5], it was argued that the word "income" should be construed as including only such income as constitutes or provides a profit or gain to the recipient, *i.e.*, that the word "income" is in some way limited by its association with the words "profits" and "gains." Their Lordships, however, held that they agreed with the opinion expressed by the learned Chief Justice of the Patna High Court that the word "income" was not limited by the words "profits" and "gains" and anything which could properly be described as income was taxable under the Act unless expressly exempted.

Section 4 (2) of the Indian Income-tax Act engrafts an exception to this general rule and it provides that in the case of a wife resident in British India who receives remittances from her husband who is not resident in British India out of any part of his income which is not included in his total income the remittances so received shall be deemed to be income

(1) [1903] 1 K.B. 405, at pp. 411-412.
(2) (1894) 3 Tax Cas. 306, at p. 308.
(3) [1896] 2 Q.B. 179, at p. 184.
(4) (1932) 59 Cal. 1343; 1932 A.L.J. 588.
(5) [1935] 3 I.T.R. 237.

accruing in British India to the wife. There can be no doubt, therefore, that the sums received by the assessee from Kalsia are to be deemed to be income of the assessee which has accrued to her in British India. For the purposes of that sub-section three conditions are necessary, firstly, that the husband was not resident in British India, secondly, that he should have made remittances which were received by his wife resident in British India, and lastly, that such remittances should have been made out of any part of his income which is not included in his total income. If these three conditions are fulfilled, then the remittances received must "be deemed to be income accruing in British India to the wife." It will be noticed that the word here used is "remittances" and there can be no doubt that the moneys received by the assessee were remittances. It was admitted by learned counsel for the assessee that in Kalsia the whole income of the State is at the disposal of the Raja although a budget is prepared for the purpose of allocating moneys to different heads of expenditure. It is all Raja's money to be spent as he pleases and there is no constitution which makes any sharp distinction between the Raja's privy purse and the rest of the income which does not belong to him and cannot be touched by him. The moneys, therefore, received by the assessee, though provided for in the State budget, must be deemed to be remittances received by his wife. It is also not disputed that the wife, the assessee, is a resident in British India, while the Raja is not a resident in British India. Lastly, the question is whether the remittances were made out of any part of the income of the Raja which was included in his total income.

All the members of the Tribunal were of the opinion that Section 4 (2) was not applicable because "the husband has not been assessed to income-tax" on his total income. To my mind, the section has been completely misunderstood by the members of the Tribunal. I have already in the earlier part of my judgment said that a non-resident is liable to pay tax for moneys which he has received in British India or which is deemed to have been received by him in British India. To my mind, Section 4 (2) is an extension of that principle and what is attempted is, to tax such income when it is not received by the husband in British India but is received by his wife in the shape of remittances received in British India. The provision that such remittances should not be out of any part of his income which is included in his total income is obviously for the purpose of avoiding double taxation. I can find no reason why the remittances received by the wife should be taxable only when the remittances are made from other income, but the husband has some income which can be included in his total income and not when he has no income which can be included in his total income. All that the section requires is that the remittances should be from income not included in his total income and obviously in the latter

case the remittances must be from income which is not included in his total income. There can be no doubt that no part of the money out of which these remittances have been made was included or could be included in the total income of the Raja for the purposes of the Indian Income-tax Act and it is, therefore, clear to me that the remittances received by the wife are taxable as receipts "deemed to be" income accruing to her in British India.

Learned counsel has argued that a gift of money is never taxable as income in the hands of the donee. He has in support of this proposition cited before us Halsbury's Laws of England, Hailsham Edition, volume 17, page 14, paragraph 16, and again page 265, paragraph 531. Apart from the question that little can be gained by trying to construe an Income-tax Act of one country in the light of a decision upon the meaning of the income-tax legislation of another, as was remarked by their Lordships of the Judicial Committee in *Gopal Saran Narain Singh* v. *Commissioner of Income-tax* [1], the proposition, to my mind, as stated by learned counsel, is far too general. I shall deal with this matter in greater detail when I come to deal with the question of allowances paid to the assessee from the Nabha State. In Section 4, sub-section (2), the legislature has laid down that the remittances received by the wife in British India are taxable as income which has accrued to the wife in British India. The word "remittances" means sending of money. There can be no doubt that the moneys received by the assessee were remittances to her within the meaning of Section 4, sub-section (2), and, therefore, they shall be deemed to be income which has accrued to the wife in British India. The last point urged in this connection was that the remittances being voluntary must be deemed to be of a casual and non-recurring nature as the husband had the right to stop the remittances at any moment he liked. Section 4 (2) is in the nature of an exception to Section 4 (1) which is the general section and, to my mind, the exceptions in Section 4 (3) cannot be engrafted on Section 4 (2) and the question about the remittances being of a casual and non-recurring nature, therefore, does not arise.

There is further reason for this conclusion. If the husband had himself come to Dehra Dun and received these moneys in Dehra Dun, it could not be urged that the receipts by him were of a casual and non-recurring nature. There was a definite source, *viz.*, the income of his State, from which moneys were bound to come to him and the amount could, therefore, be taxed in his hands as his income, provided he could not claim exemption from taxation under the international law on the basis of his being sovereign. I have already held that Section 4, sub-section (2), is an extension of this principle and for the purposes of that section the amount is taxable, even though it is not the husband but the wife who has received it.

(1) [1935] 3 I.T.R. 237, at p. 242.

I am, therefore, of the opinion that the amounts received by the assessee from the Raja of Kalsia are taxable as income which must be deemed to have accrued to the assessee in British India under Section 4 (2) of the Indian Income-tax Act and that no question as to whether they are casual and non-recurring arises.

Next arises the question of the allowances made by the Nabha State. The findings of fact recorded by the Tribunal are that there is a practice of making allowances by the Ruling Prince to his sister and to his other dependents, but this depends entirely on his will and pleasure, that is, if the Maharaja of Nabha at any time chose to stop the allowance, the assessee would have no right to claim it from him either in the British Courts or in his own Courts. Learned counsel has argued that the allowances made to the assessee were not income at all, and he has relied on Halsbury's Laws of England, Hailsham Edition, volume 17, page 14, paragraph 16, which is in these words :—

"Unless gifts or voluntary allowances are part of the emoluments of an office, employment or vocation, they are not income . . ."

and at page 265, paragraph 531, of the same volume :—

"Gifts or voluntary allowances are not income in the hands of the recipient unless they are attached to and form part of the emoluments of an office, employment, or vocation."

This matter is further discussed in the same volume from paragraphs 435 to 438 at pages 213-217. Before accepting the proposition enunciated above, we must bear in mind that the scheme of the Indian Income-tax Act is entirely different from the scheme of the English Act. Under the latter Act the profits and gains that are taxable are set out in the various schedules to the Act and before a tax can be levied the profits and gains which are sought to be taxed must fall under one or other of the heads specified in the schedules. On the other hand, under the Indian Income-tax Act all income, profits and gains are made taxable unless they fall within the exceptions mentioned in the Act. After having enumerated the four heads of "salaries, interest on securities, income from property," and "profits and gains of business, profession or vocation," the Act provides the last head of "income from other sources." Section 4, sub-section (1), makes it clear that such income may be from whatever source derived, and Section 12 says that it may be of every kind which is not included in any of the preceding heads. It will, therefore, be unsafe to go by mere analogy of the English Act, and their Lordships of the Privy Council have in two cases, *Commissioner of Income-tax, Bengal* v. *Shaw Wallace & Co.*[1] and *Gopal Saran Narain Singh* v. *Commissioner of Income-tax*[2], warned the Courts against construing the Indian Income-tax Act in the light of decisions upon

(1) (1932) 59 Cal. 1343; 1932 A.L.J. 588. (2) [1935] 3 I.T.R. 237.

the meaning of income-tax legislation of other countries. In the latest decision in *Kamakshya Narain Singh* v. *Commissioner of Income-tax, Bihar and Orissa* [1], their Lordships have, at page 496, observed:—

"The Indian Income-tax Act of 1922, which was a consolidating Act, is both in its general framework and its particular provisions different from the English Income Tax Acts, so that decisions upon the English Acts are in general of no assistance in construing the Indian Act. But on some fundamental concepts reference may be to some extent usefully made to English decisions, in particular as to the meaning of the word 'income'."

In view of this observation it may have been necessary to consider what was the meaning of the word "income" under the English Statute. Their Lordships have, however, themselves attempted to define the word "income," but as they have pointed out that when the legislature did not define the word "income," it did not do so because there could be no definition which would be entirely satisfactory. What is taxable income of an assessee would differ in each case according to the facts and circumstances of that case. This may be illustrated by the following example which is given in one of the decisions of their Lordships of the Judicial Committee. A person who owns certain shares wants to sell them with the object of either obtaining cash or with the object of investing the money in fresh securities. He sells those shares and gets money for them. The shares are sold at a premium. The difference between the purchase price and the sale price would not ordinarily be taxable as it is an augmentation of the capital. If, on the other hand, a person, who is a regular share dealer and speculates in shares on the stock exchange by judicious buying and selling of shares, has in the course of the year made a lakh of rupees as profit, there can be no doubt it will be treated as his income and, as such, be taxable.

The leading case on the subject which attempted to define this most difficult word "income" is the decision of their Lordships of the Judicial Committee in *Commissioner of Income-tax, Bengal* v. *Shaw Wallace & Co.* [2] There the assessees were given a certain solatium for the compulsory cessation of their business as agents, and the question was whether the payment thus made was in the nature of a capital receipt or was it a receipt from business or other sources which were taxable. Their Lordships held that income should be (1) in the nature of a periodical monetary return (2) "coming in" with some sort of regularity and (3) from definite sources, the source being not necessarily one which is expected to be continuously productive, but it must be one whose object is the production of a definite return, excluding anything in the nature of a mere windfall. It must be remembered that this definition was given by their Lordships when

(1) (1943) A.L.J. 493; 11 I.T.R. 513, at p. 518. (2) (1932) 59 Cal. 1343; 1932 A.L.J. 588.

dealing with the question whether the amount paid to the assessees was in the nature of a capital receipt or was an income from business. Their Lordships held that it was not an income from business. It is true that dealing with the question whether it was income from other sources their Lordships held that the reasoning previously given by them applied to that question also and the payment was in the nature of a solatium which was a windfall and was not an income at all. This definition has been accepted by the Courts in India, as it was bound to be, as the leading case on the definition of the term "income." In the next case before their Lordships, *Gopal Saran Narain Singh* v. *Commissioner of Income-tax*[1], where the question was whether an annuity payable under an agreement for consideration amounted to a payment of the purchase price by instalments, it was held that the annuity was not a capital asset but was taxable income under the head "other sources." Their Lordships reaffirmed and accepted the definition of the word "income" as given in the decision of the case in *Commissioner of Income-tax, Bengal* v. *Shaw Wallace & Co.*[2] and quoted it with approval. Both these cases, it must be remembered, were cases where the question was whether the money received by the assessee was in the nature of a capital receipt or was taxable income. The latest case is the case in *Kamakshya Narain Singh* v. *Commissioner of Income-tax, Bihar and Orissa*[3], where the question was whether the royalties realised from lessees of coal mines under certain leases were in the nature of capital payments or were taxable income. Their Lordships held, relying on the terms of the lease, that the sources of "the royalties may properly be deemed to be *the lessees' covenants to pay them*, and hence royalties fall under 'other sources'." Their Lordships, while dealing with the meaning of the word "income," observed:—

"Income, it is true, is a word difficult and perhaps impossible to define in any precise general formula. It is a word of the broadest connotation. Its definition has, however, been approached in recent decisions of this Board. The first to which their Lordships think it is desirable to refer is *Commissioner of Income-tax, Bengal* v. *Shaw Wallace & Co.*[2]"

Their Lordships then quoted the definition given in *Commissioner of Income-tax, Bengal* v. *Shaw Wallace & Co.*[2] and went on:—

"That definition was followed and in substance repeated in a decision of the Board delivered by Lord Russell of Killowen in *Gopal Saran Narain Singh* v. *Commissioner of Income-tax*[1]......Lord Russell, adopting generally the definition already quoted, added the following important amplification:

'The word 'income' is not limited by the words 'profits' and 'gains.' Anything which can properly be described as income, is taxable under the Act unless expressly exempted.'"

(1) [1935] 3 I.T.R. 237.
(2) (1932) 59 Cal. 1343; 1932 A.L.J. 588.
(3) [1943] 11 I.T.R. 513; 1943 A.L.J. 493.

Their Lordships then observed :—

"It is not in their Lordships' opinion correct to regard as an essential element in any of these or like definitions a reference to the analogy of fruit, or increase or sowing or reaping or periodical harvests. Lord Cairns (*loc. cit.*) used these expressions because he was distinguishing mineral leases from agricultural leases. Sir George Lowndes (*loc. cit.*) speaks of 'income' being likened pictorially to the fruit of a tree or the crop of a field. But it is clear that such picturesque similes cannot be used to limit the true character of income in general, and particularly when it is constituted by mining rent or royalties."

Then their Lordships go on to hold :—

"Income is not necessarily the recurrent return from a definite source, though it is generally of that character. Income again may consist of a series of separate receipts, as it generally does in the case of professional earnings. The multiplicity of forms which 'income' may assume is beyond enumeration. Generally, however, the mere fact that the income flows from some capital assets, of which the simplest illustration is the purchase of an annuity for a lump sum, does not prevent it from being income, though in some analogous cases the true view may be that the payments, though spread over a period, are not income, but instalments payable at specified future dates of a purchase price. Such a case is illustrated by *Scoble* v. *Secretary of State for India* [1]."

As regards the argument of learned counsel that a gift is not taxable at all, I may mention that many gifts or voluntary payments are made expressly taxable by the Indian Income-tax Act itself, or, at any rate, it contemplates the possibility of their being taxed, for example, in Section 4 (3) (ii) any income of a religious or charitable institution derived from voluntary contributions, and applicable solely to religious or charitable purposes is not taxable which implies that if it is not applied solely to religious or charitable purposes it would probably be taxed. Further, any annuity or even a gratuity paid to a servant is taxable under the head "salaries." It is true that in construing the Income-tax Act it is not always safe to deduce from an exemption that the contrary must be taxable income. There are certain classes of income made expressly taxable and certain exemptions separately mentioned to override or overrule the decisions of the Courts which did not find favour with the legislature, or it may be that they are expressly mentioned due to the over-anxiety of the draftsman to make the point clear beyond all possibility of doubt. Referring to the argument that Section 4 (3) (v) suggests that the word "income" in the Act may have a wider significance than would ordinarily be attributed to it, their Lordships of the Judicial Committee have expressed the view, in

(1) [1903] A C. 299.

Commissioner of Income-tax, Bengal v. *Shaw Wallace & Co.*[1], that they do not think that any of the sums mentioned in that clause, apart from their exemption, could be regarded in any scheme of taxation as income and they think that the clause must be due to the over-anxiety of the draftsman to make this clear beyond any possibility of doubt. It is, however, not necessary to pursue this matter further as the question really is whether the remittances made by the Maharaja of Nabha to the assessee are her income or are taxable income. I am inclined to hold that in any case the remittances are not taxable income. The remittances made by the Maharaja of Nabha to the assessee may be income but to my mind they are expressly exempted under Section 4, clause (3) (vii). That sub-clause provides that any receipts not being receipts arising from business or the exercise of a profession, vocation or occupation, which are of a casual and non-recurring nature, or are not by way of addition to the remuneration of an employee are not taxable.

There can be no doubt that the allowances made by the Maharaja of Nabha to the assessee were of a casual nature. The case in *Stedeford* v. *Beloe*[2] dealt with the question whether the allowances and pensions, given to the headmaster of a school on his retirement when his service was not a pensionable service and the pension depended entirely upon the goodwill of the governing body, who might at any time, if they wished, rescind the minute under which they granted the pension, fell under Schedule E, Income Tax Act of 1918, as amended by Section 18, Finance Act, 1922. Viscount Dunedin observed :—

"......it has been held again and again that a mere voluntary gift is not such a profit because it is not, in the true sense of the word, income. It is merely a casual payment which depends upon somebody else's goodwill."

Lord Warrington of Clyffe observed :—

"Here each payment is wholly voluntary. The case is only an instance of a succession of voluntary payments, each of which is voluntary and none of which need necessarily be continued."

Lord Thankerton said :—

"It was a mere donation, given each year with no certioration that it would be repeated the year following."

In that case the pension was not an instance of an isolated payment but a series of payments, and yet Viscount Dunedin characterised it as a mere casual payment which depended upon somebody else's goodwill. That decision of the House of Lords, to my mind, conclusively establishes that the payments made by the Maharaja of Nabha to the assessee, depending as they did on the pleasure of the donor, were "casual" payments. It is,

(1) (1932) 59 Cal. 1343; 1932 A.L.J. 588. (2) [1932] A.C. 388.

however, argued on behalf of the Department that the fact that the payment has been regularly made during the last six years before the year of assessment showed that it was not of a non-recurring nature and Section 4 (3) (vii) requires that for the purpose of exemption not only the payment should be "casual" but that it should also be of a "non-recurring nature." In none of the cases cited before us have the words "non-recurring nature" been considered by the Judicial Committee or by any Court in India. As I understand those words, they mean not that the payment has, as a matter of fact, recurred but that it was bound to recur. If the Maharaja of Nabha had in any one year made a present of a sum of money to his sister, it is conceded that it would not be taxable income as it would be of a casual and non-recurring nature. If it is made a second time, it is said that that too may be casual and non-recurring, but if the payment is repeated a third or a fourth or a fifth time, from the fact of the repetition itself it is said the Courts may be able to deduce that it was not a mere casual payment of a non-recurring nature and was, therefore, not exempt from taxation. To my mind, the word "non-recurring" does not mean that it has, as a matter of accident or as a matter of fact, recurred, but that there was a claim or a right in the assessee to expect its recurrence. I think a mere voluntary payment, not being receipts arising from business or the exercise of a profession, vocation or occupation and not being by way of addition to the remuneration of an employee or not having been made expressly liable, is not liable to be taxed; and as I understand the exception, a voluntary payment must be deemed to be of a casual and non-recurring nature unless there is a liability on the donor to pay, which liability may arise out of a contract, a custom or some order which is binding on him.

On the grounds given by me above I would hold that the allowances made to the assessee from Nabha do not constitute her personal income assessable under the Indian Income-tax Act and that they are of a casual and non-recurring nature and are, as such, exempt under Section 4 (3) (vii) of the Act. To my mind, there was no justification in splitting up questions Nos. (1) and (2) into parts (a) and (b) as they appear to me to be contradictory to each other. If the case fell under Section 4 (3) (vii) of the Act, it would necessarily not be personal income assessable under the Indian Income-tax Act, and I, therefore, do not see any reason why the questions were split up as they have been. To my mind, questions (1) and (2) may have been better framed in the words of the Privy Council in *Commissioner of Income-tax, Bengal* v. *Shaw Wallace & Co.*[1], that is, whether the moneys received by the assessee from Kalsia were in the nature of an income receipt and would fall to be assessed to income-tax? A similar question may have been framed with reference to the receipts from Nabha.

(1) (1932) 59 Cal. 1343; 1932 A.L.J. 588.

The last question that we have to consider now is whether the assessee being the wife of the Ruling Chief of Kalsia is exempt under the canons of international law from taxation under the Indian Income-tax Act in respect of her personal income accruing, arising or received in British India. The question presupposes that the Raja of Kalsia is a Ruling Chief and there is no question separately addressed to us whether the relationship for the purpose of taxation between the Raja of Kalsia and the Income-tax Department is to be regulated by considerations of international law. The point was argued before us at great length, though in the view that I have taken it is not necessary to express any definite opinion on the point. I am of the opinion that even if the Raja of Kalsia was an independent sovereign and exempt from payment of income-tax in British India, his wife was not so exempt. The Central Government has been given authority by Section 60 of the Indian Income-tax Act to make an exemption, reduction in rate or other modification, in respect of income-tax in favour of any class of income, or in regard to the whole or any part of the income of any class of persons. Such power is to be exercised by a notification in the Official Gazette. It is admitted that no such notification in favour of the Ruling Chiefs has been made by the Government of India. It is, however, argued that on the well recognised principle of international law, *par in parem non habet imperium*, a foreign sovereign is not entitled to be taxed by the Government of another country, and in support of that principle learned counsel has cited before us Oppenheim's International Law, volume I, 5th edition, pages 590 and 591. It is not denied that the legislature of an independent State has the power to override by appropriate legislation a rule of international law: see the observations in *Rochefoucauld* v. *Boustead*[1]. It is argued that unless the rules of international law have been expressly abrogated by statute, the Courts would interpret the Act, as far as its language admits, so as not to be inconsistent with the established rules of international law or with the principles of comity of nations: see Maxwell on Interpretation of Statutes, 7th edition, page 127. There can be no doubt that these are sound principles of law and in interpreting the Income-tax Act it must be conceded that there is nothing in the language of the Act which would entitle us to hold that the legislature intended to override any settled principles of international law.

The distinction between British territory in India or British India and the territory of the Indian States is well recognised, and it is admitted on all hands that the Indian States do not form a part of the British territory, though the Crown exercises certain rights through His Majesty's representative known as the Crown Representative including the right of conducting international relations, the right of exercising jurisdiction over

(1) (1897) 66 L.J. Ch. 74.

Europeans and Americans, interference to settle disputes as to succession to the State, the suppression of grave misrule in the State, and the regulation of armaments and the strength of military forces. The question whether the Indian States can be called sovereign States merely because they exercised internal sovereignty is not free from doubt. It is recognised by some of the text-writers on international law that a State may exist *qua* State, *i.e.*, retain its "political personality," notwithstanding a very great "*imminutio imperii*" resulting from its relation with other States or with a more powerful State. In spite of the fact that certain text-writers have expressed an opinion against the Indian States being sovereign States, the Courts have so far disclaimed all jurisdiction against a Ruling Chief. Hall in his book on International Law, page 28, Westlake in his Collected Papers for International Law, page 216, and Smith in his International Law, page 59, have all expressed the view that Indian States are not subjects of international law. Oppenheim has drawn a distinction between a vassal State and a protected State and is of opinion that the Indian States are all vassal States. The question of the liability to pay income-tax on the income of property situate in British India and owned by an Indian State arose in *Bishwanath Singh* v. *Commissioner of Income-tax, Central and United Provinces*[1]. Mr. Pathak on behalf of the assessee has attempted to distinguish that case on the ground that the status of the Raja of Kalsia was different from the status of the Maharaja of Benares. According to him the sovereign rights of the Maharaja of Benares flowed from an Instrument of Transfer, dated 1st April, 1911 (see Aitchison's Treaties, Engagements and Sanads, volume 2, page 89), and with respect to territories which were not included in the Benares State it was provided that "within the other estates now in possession of His Highness Sir Prabhu Narayan Singh, G. C. I. E., which are outside the State of Benares, he shall continue to have the status and responsibilities of a land-holder under the ordinary law and within the pargana of Kaswar Raja he shall assume that status and those responsibilities."

It is argued that with reference to house property in British India his position was that of any other owner and he could be taxed. It is further urged that the Maharaja of Benares having derived his sovereignty under the Instrument of Transfer of 1st April, 1911, whatever rights were not transferred to him under that treaty still vested in the British Crown. As against that it is argued that the relations between the Kalsia State and the British Government are governed by treaty rights and the Kalsia State retains sovereign powers limited only by the clauses of the treaty. Moghul Emperors, in the days when they were in power, claimed to be the Emperors of Hindusthan and insisted on being recognised by the minor kings and

(1) [1942] 10 I.T.R. 322 ; 1942 A. L. J. 543.

chieftains as their overlord or sovereign, though these minor kings enjoyed a considerable amount of internal sovereignty. As the powers of Moghul kings declined their hold on these chiefs or chieftains gradually grew weaker and new chiefs or chieftains arose, but in name the kings of Delhi remained their overlord or sovereign. As the Mahratta power in the country increased, the power of the Moghul Emperors declined and ultimately about the year 1760 the Moghul Emperors became practically puppets in the hands of the Mahrattas. Thereafter they remained the virtual prisoners in the hands of the British till Bahadur Shah II was tried and formally deposed and deported after the Mutiny of 1857 and the claim for paramountcy of the Moghul Emperors was transferred to the British Crown, see State, 21 and 22 Vic., Chapter 106, which enacted

"that all territories in the possession or under the Government of the Company, *and all rights vested in* or which (if the Act had not been passed) might have been exercised by the Company *in relation to any territories* should become vested in Her Majesty."

Before the fall of the Moghul Empire, in theory at any rate, there were three independent States in India—the Moghul Empire, the kingdom of Maharaja Ranjit Singh in the Punjab and the Mahratta Confederacy. The Cis-Sutlej States were on the east of the Punjab and were not included within the kingdom of Maharaja Ranjit Singh. The State of Kalsia was founded by Sardar Gurbakhsh Singh and was one of the Cis-Sutlej States. Gurbakhsh Singh had been succeeded by his son, Jodh Singh. Sir David Ochterlony issued a proclamation on 3rd May, 1809, offering protection to the Cis-Sutlej States and guaranteed that the Chiefs who accepted the British protection shall remain in the exercise of the same rights and authority within their own possession which they enjoyed before they were taken under British protection. After some hesitation Jodh Singh decided to follow the example of the others and was also assured of protection, and treaties guaranteeing protection against Ranjit Singh were entered into with nine States including Nabha, Patiala, Kalsia, Alwar, etc.: see Lee Warner's Native States of India, 1910 edition, page 55. The treaty is set out in Aitchison's Treaties, volume 8, at pages 186 and 294. The Chief of Kalsia received an adoption Sanad in 1862 and the State was transferred to the political charge of the Commissioner of Ambala Division in the year 1912. Before that it was under the political superintendence of the Commissioner of the Delhi Division. In 1916 the hereditary title of Raja was conferred, though the Raja is not entitled to any salute of guns or to the title of His Highness.

To my mind, the difference which is attempted to be drawn by learned counsel for the assessee between an Indian State, the connections between which and the British started with a treaty, and the States which had

fought and lost and were then recognised as feudatory Chiefs of Ruling Princes, has no substance. The question whether by reason of the fact that these Indian States which enjoyed internal sovereignty subject to the paramountcy of the Crown are to be treated as foreign sovereigns who are not amenable to the jurisdiction of the British Courts has arisen in several cases. It is true that under Section 57 of the Evidence Act, a Court may, on all matters of public history or the existence of title and national flag of every State or sovereign recognised by the British Crown, resort for its aid to appropriate books or documents of reference, and most of the text-writers are of opinion that for the purposes of international law the Indian States cannot be treated as international units. The Crown has, however, always drawn a distiction between the territories in its possession and the territories of Ruling Chiefs over which it exercises rights of paramountcy. Before we come to the statutes where the sovereign status of the Indian Princes have been recognised, I may mention some of the cases where the question arose. In *Statham* v. *Statham*[1], the question arose whether His Highness the Gaekwar of Baroda could be cited as a co-respondent before the British Court. Bargrave Deane, J., at page 96 observed :—

"Grotius (De Jure Belli ac Pacis) says unequal leagues are made not only between the conquerors and the conquered, but also between peoples of unequal power, even such as never were at war with one another. Grotius, Pufendorf, and Vattel agree that in unequal alliances the inferior power remains a sovereign State. Its subjects or citizens owe allegiance only to their own sovereign. Over their disputes and internal dissensions the suzerain power as such has no jurisdiction. In short, the weaker power may exercise the rights of sovereignty so long as by so doing no detriment is caused to the interests or influence of the suzerain power. It follows that the inferior power must in all alliances with other States be controlled by its suzerain.

Vattel says a weak State which in order to provide for its safety places itself under the protection of a more powerful one and engages to perform in return several offices equivalent to that protection, without, however, divesting itself of the right of government and sovereignty, does not cease to rank among the sovereigns who acknowledge no other law than the law of nations."

It will be noticed that no distinction is drawn between a State which was conquered and a State which acknowledged its weakness and entered into a treaty and parted with certain of its sovereignty rights. It was held in that case that the Maharaja of Baroda was a sovereign Prince and could not be sued in a British Court. The matter arose before the House of Lords in *Duff Development Co., Ltd.* v. *Government of Kelantan*[2]. The

(1) (1912) L.R. 1912 P. 92. (2) [1924] A.C. 797.

position of the State of Kelantan was analogous to the position of the Indian States, yet their Lordships held that :—

"A government recognised as sovereign by His Majesty's Government is not the less exempt from the jurisdiction of our Courts because it has agreed to restrictions on the exercise of its sovereign rights."

The same point again arose in *Jwala Prasad* v. *Rana of Dholpur* [1]; *Sirdar Gurdyal Singh* v. *Raja of Faridkot* [2]; *Movstak Rae* v. *Lady Randheer Singh of Kapurthala State* [3]; *Lachmi Narain* v. *Raja Partab Singh of Rampur* [4]; *Ladkuverbai* v. *Ghoel Shri Sarangji Pratabsangji* [5]; the case relating to the Thakur of Palitana, *Phumanlal* v. *Raja Shamsher Parkash* [6] and *Beer Chunder* v. *Nobodeep Chunder Deb* [7]. In all these cases it was held that Ruling Chiefs of Indian States were sovereign Princes and were not amenable to the jurisdiction of civil Courts in British India. To my mind, the decision in *Bishwanath Singh* v. *Commissioner of Income-tax, Central and United Provinces* [8], does not go against that principle. Under the international law a foreign sovereign, an ambassador and an envoy of a foreign Government enjoy immunity from taxation. Any immovable property, even though it may be owned by a foreign sovereign, is under the jurisdiction of the Court of that country. It is only to be deemed as foreign territory when it is the official residence of the sovereign or his ambassador. The income of the house property owned by the Maharaja of Benares over which income-tax was held to be payable in *Bishwanath Singh* v. *Commissioner of Income-tax, Central and United Provinces* [8], was not income from such property which could be said to be outside the jurisdiction of the Indian Courts.

The Indian States have been recognised as sovereign States by various statutes in India and in England. Under the Civil Procedure Code beginning from 1859 the restriction of the British Courts over Indian Princes has been well recognised. The present Sections 85 and 86 of Act V of 1908 make Indian Princes liable to be sued on three grounds which are exactly the same as under the well recognised principles of international law, that is, if they have immovable property in British India and the suit is brought with reference to that property, if they have themselves brought a suit and brought themselves under the jurisdiction of the British Courts, and lastly, if they trade within the local limits of the jurisdiction of the Court; and such suit can only be brought with the consent of the Governor-General in Council. A reference to Sections 85, 86 and 87 would show that a sovereign Prince and a Ruling Chief of an Indian State are placed exactly on the same footing. The Foreign Jurisdiction Act, 53 and 54 Vict.

(1) [1863] S.D.A. 579.
(2) [1894] A.C. 670.
(3) (1870) 54 P.R. 1870.
(4) (1878-80) 2 All. 1.
(5) (1870) 7 Bom. H.C.R. 150.
(6) (1875) 93 P.R. 1875.
(7) (1883) 9 Cal. 535, at p. 552.
(8) [1942] 10 I.T.R. 322; 1942 A.L.J. 543.

Chapter 37, was made applicable to the Indian States by an Order in Council, dated 11th June, 1902.

Section 4 (3) of the Indian Income-tax Act was amended by the Indian Income-tax (Amendment) Act (XXIII of 1941), and a sub-clause (*x*) was added, and it was made clear that an accredited representative in British India for political purposes of a Ruling Chief is not liable to pay income-tax on any remuneration received by him in such capacity. That sub-section, to my mind, recognises in part the rule of public international law that an ambassador of a foreign State is not liable to pay tax in the country where he may be posted by his Government. Further under Section 49A of the Act, which was added by the Indian Income-tax (Amendment) Act (VII of 1939), the Central Government may, by notification in the official Gazette, make provision for the granting of relief in respect of income on which has been paid both income-tax (including super-tax) under this Act and Dominion income-tax, and "Dominion income-tax" has been defined to include any income-tax or super-tax charged under any law in force in any Indian State. These provisions in the Indian Income-tax Act incline me to the view that the legislature recognised that the territory of the Indian States was outside British India and the Ruling Chief of an Indian State was a sovereign Prince who had the same immunity from taxation as any other foreign sovereign.

Learned counsel has drawn our attention to Section 47 of the Government of India Act where the word "sovereignty" has been used with respect to certain territories of His Exalted Highness the Nizam of Hyderabad. That the Kalsia State is an Indian State within the meaning of Section 3 (27) of the General Clauses Act of 1897 and Section 311 of the Government of India Act of 1935 admits of no doubt. The President of the Appellate Tribunal, Mr. M. Munir, was of the opinion that he was bound to hold "that the Kalsia State is not a subject of international law and its Ruler not an independent sovereign." Mr. Yahya Ali, with whom the other two members of the Tribunal, Mr. A. L. Sahgal and Mr. N. N. Chakravarty, agreed, held as follows :—

"It is from the authorities abundantly clear therefore that the appellant's husband as a Ruler of Kalsia is not entitled to the rights of extra-territoriality (including the right of exemption from taxation) which a sovereign is entitled to under the code of international law."

All the members of the Tribunal were, therefore, agreed that the Ruler of Kalsia was not entitled to immunity from taxation under the international law. So far as I can see, the question has not been referred to us for our opinion. The question reads as follows :—

"Whether, by reason of her being the wife of the Ruling Chief of Kalsia, the assessee, who is a resident in British India, is exempt under the

canons of international law from taxation under the Indian Income-tax Act, in respect of her personal income accruing, arising or received in British India."

If I had to consider the question whether the Ruling Chief of Kalsia was exempt from taxation under the international law, as at present advised, I would probably have held against the Commissioner of Income-tax. One point that strikes me at the outset is that if it were held that a Ruling Chief is not exempt under the Indian Income-tax Act, then if he were to become resident in British India, as defined in Section 4A of the Act, his total income would have included not only the amounts that were received by him or had accrued to him in British India but all such income which may have accrued to him in that year even without British India and on that basis he might have been called upon to pay income-tax on the total revenue of his State. The proposition has only to be rejected as absurd. I may point out that by the Indian Income-tax (Amendment) Act (XXIII of 1941) a new clause (c) was added to Section 14 (2) which reads as follows:—

"The tax shall not be payable by an assessee—in respect of any income, profits or gains accruing or arising to him within an Indian State, unless such income, profits or gains are received or deemed to be received in or are brought into British India in the previous year by or on behalf of the assessee, or are assessable under Section 42."

This exemption did not come into force before 1st April, 1944, and before this amendment therefore the Ruling Chief resident in British India could easily have been taxed on the total income of his State unless it could be said that he was exempt by reason of the fact that he was a sovereign Prince. Learned counsel for the Department has relied on Section 155 of the Government of India Act, 1935, and has urged that it presupposes the liability of the Indian States to taxation, but that section only relates to Federal taxes and it refers to only those States which had decided to come within the Federation under Section 5 of the Act. The portion of the Act dealing with Federation has not yet come into effect. The argument that the wife of a sovereign is exempt from taxation is based on certain observations in Oppenheim's book on International Law, volume I, pages 590-591. He says:—

"The wife of a sovereign must likewise be granted ex-territoriality, but not other members of a sovereign's family."

Oppenheim based it on the authority of Rivier, while according to Bluntschli, ex-territoriality need not in strict law be granted to the wife of a sovereign. A reference to Sections 85 and 86 of the Civil Procedure Code (V of 1908) would, however, show that there is no such protection given to the wives of Indian Princes against their liability to be sued in British

India. The only case in which the question of the wife of an Indian Chief being sued arose was the case in *Movstak Rae* v. *Lady Randheer Singh of Kapurthala State*[1]. A reference to that case, however, would show that the suit had been filed with reference to moneys lent to Lady Randheer Singh, Rani of Kapurthala, while she was living inside the State with the Maharaja. The suit was brought in British India where she happened to be present and the Court held that the cause of action had arisen in the State and the Court would not entertain a suit between a State subject and the Ruler or his wife on a cause of action which had accrued inside the State and outside British India merely on the ground that the defendant happened to be in British India. A reference to Section 155 of the Government of India Act, 1935, would also show that the exemption from Federal taxation with respect to lands, or buildings situate in British India or income accruing, arising or received in British India is given only to the Ruler of a Federated State and not to his wife.

Learned counsel for the assessee has argued that in case of doubt the benefit of the doubt must go to the assessee and his client must, on the opinion of Rivier, be given the exemption. I am, however, inclined to follow the opinion of Bluntschli whose opinion seems to have been tacitly accepted in the Civil Procedure Code and in the Government of India Act. If the wife of a Ruling Chief is not exempt and can be sued in British Courts, there seems to be no principle under which we can say that she is exempt from taxation.

Our attention was also drawn to the Government Trading Taxation Act of 1926 and it was urged that if Indian Princes were liable under the Indian Income-tax Act, it was unnecessary to have the Government Trading Taxation Act of 1926 on the Statute. Dr. Asthana on behalf of the Department has argued that the Government Trading Taxation Act was intended to include not only the Indian States but any part of His Majesty's dominions exclusive of British India. That may be so, but there can be no doubt that the Government Trading Taxation Act of 1926 was intended to include not only His Majesty's dominions but also the Government of the Indian States trading in British India and that, to my mind, is some indication that the Ruling Chiefs of Indian States, as such, are not liable to taxation under the Indian Income-tax Act. However, in the view that I have taken that the wife of an Indian Chief is not entitled to the same exemption, it is not necessary for me to go into the question of the liability of the Ruling Chiefs any further. My answer to the question, therefore, is in the negative.

IQBAL AHMAD, C. J.—I have had the advantage of reading the judgment of my brothers Braund and Malik and I agree with the conclusions arrived

(1) (1870) 54 P.R. 1870.

canons of international law from taxation under the Indian Income-tax Act, in respect of her personal income accruing, arising or received in British India."

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India. The only case in which the question of the wife of an Indian Chief being sued arose was the case in *Movstak Rae* v. *Lady Randheer Singh of Kapurthala State* [1]. A reference to that case, however, would show that the suit had been filed with reference to moneys lent to Lady Randheer Singh, Rani of Kapurthala, while she was living inside the State with the Maharaja. The suit was brought in British India where she happened to be present and the Court held that the cause of action had arisen in the State and the Court would not entertain a suit between a State subject and the Ruler or his wife on a cause of action which had accrued inside the State and outside British India merely on the ground that the defendant happened to be in British India. A reference to Section 155 of the Government of India Act, 1935, would also show that the exemption from Federal taxation with respect to lands, or buildings situate in British India or income accruing, arising or received in British India is given only to the Ruler of a Federated State and not to his wife.

Learned counsel for the assessee has argued that in case of doubt the benefit of the doubt must go to the assessee and his client must, on the opinion of Rivier, be given the exemption. I am, however, inclined to follow the opinion of Bluntschli whose opinion seems to have been tacitly accepted in the Civil Procedure Code and in the Government of India Act. If the wife of a Ruling Chief is not exempt and can be sued in British Courts, there seems to be no principle under which we can say that she is exempt from taxation.

Our attention was also drawn to the Government Trading Taxation Act of 1926 and it was urged that if Indian Princes were liable under the Indian Income-tax Act, it was unnecessary to have the Government Trading Taxation Act of 1926 on the Statute. Dr. Asthana on behalf of the Department has argued that the Government Trading Taxation Act was intended to include not only the Indian States but any part of His Majesty's dominions exclusive of British India. That may be so, but there can be no doubt that the Government Trading Taxation Act of 1926 was intended to include not only His Majesty's dominions but also the Government of the Indian States trading in British India and that, to my mind, is some indication that the Ruling Chiefs of Indian States, as such, are not liable to taxation under the Indian Income-tax Act. However, in the view that I have taken that the wife of an Indian Chief is not entitled to the same exemption, it is not necessary for me to go into the question of the liability of the Ruling Chiefs any further. My answer to the question, therefore, is in the negative.

IQBAL AHMAD, C. J.—I have had the advantage of reading the judgment of my brothers Braund and Malik and I agree with the conclusions arrived

(1) (1870) 54 P.R. 1870.

at by them. The answer to the questions referred should, in my opinion, be as formulated by my brother Braund.

BY THE COURT.—The answer to the questions referred is as follows: (1) The allowances received by the assessee from the Kalsia State during the accounting year should be deemed to be her income accruing in British India. No question arises in this case whether they are of a casual and non-recurring nature. (2) The moneys received by the assessee from the Nabha State during the accounting year do not constitute her personal income assessable under the Indian Income-tax Act. (3) The assessee, by reason of her being the wife of the Ruling Chief of Kalsia, is not exempt under the canons of international law from taxation under the Indian Income-tax Act, in respect of whatever is, or is deemed to be, her income accruing, arising or received in British India.

In the circumstances of the present case we direct the parties to bear their own costs of this reference. We assess the fee of the counsel for the Department at Rs. 500.

Reference answered accordingly.

[IN THE CHIEF COURT OF SIND.]

COMMISSIONER OF INCOME-TAX, BOMBAY

v.

BAI NINDHI BAI.

DAVIS, C. J., and THADANI, J. January 10, 1946.

INCOME AND CAPITAL—WILL—PROVISION THAT SUCCESSOR TO TESTATOR'S BUSINESS SHALL PAY A CERTAIN SHARE IN THE PROFITS FOR ONE YEAR TO TESTATOR'S WIFE—COMPROMISE DECREE PROVIDING FOR PAYMENT OF FIXED SUM TO HER AS LONG AS SUCCESSOR CARRIED ON THE BUSINESS—SUMS RECEIVED, WHETHER INCOME OR CAPITAL.

The assessee's husband, who had been carrying on a business, provided by his will that on his death his nephew M was to carry on the business and should give the assessee a two annas share in the net profits of the business for twelve months and thereafter as the said M may think fit and proper, M remaining the owner of the business. By a compromise decree the assessee and M agreed that instead of paying two annas share to the assessee for one year only, and thereafter whatever M liked, M shall pay to her Rs. 200 a month from the date of the death of the testator as long as M carried on business in the same premises and under the old name: Held, *that the payments received by the assessee under the compromise decree were not capital payments received in exchange for the goodwill of the business but a share in the income of the business and were assessable to income-tax.*

Cases referred to :—

Commissioner of Income-tax, Bihar and Orissa v. Gopal Saran Narain Singh [1934] (2 I.T.R. 264; 13 Pat. 661; A.I.R. 1934 Pat. 384; 151 I.C. 477; 7 I.T.C. 257).

Commissioner of Income-tax, Bombay v. Mills Store Co. [1941] (I.L.R. 1941 Kar. 512; 9 I.T.R. 642; 199 I.C. 861; A.I.R 1942 Sind 53).

Reference under Section 66 (1) of the Indian Income tax Act (XI of 1922) by the Income-tax Appellate Tribunal: Reference No. 42 of 1942.

STATEMENT OF CASE.

" This is an application by the assessee under Section 66 (1) of the Income-tax Act to refer to the Court a question of law which, it is claimed, arises from the order of the Tribunal in R. A. A. No. 5 (Sind) of 1941-42.

2. Bai Nindhi Bai, who is the petitioner in these proceedings is the widow of Seth Kakumal who was carrying on a confectionary business in partnership with Seth Motumal under the name and style of Hassomal Manghanmal. Kakumal died on 23rd April, 1932, and in his last will and testament, dated 13th April, 1932, he made a direction that on his death his wife Bai Nindhi Bai should receive a two annas share out of the net profits of the shop business for twelve months and that thereafter Motumal might do whatever he thought fit and proper. Motumal was under that direction to remain *malik* of the shop business to be done and continued under the name of Hassomal Manghanmal, the father of the testator. After her husband's death Bai Nindhi Bai instituted suit No. 228 of 1932 in the Court of the Judicial Commissioner, Sind, in which she *inter alia* challenged the aforementioned will and contended that it was either not executed by the deceased or that it was made in ignorance of its contents. That suit was in substance compromised and decreed on 21st November, 1935, in terms of that settlement. The material portion of the consent decree relating to the subject-matter of these proceedings is found in clause 6 of the decree which is reproduced below :—

' It is agreed as between the plaintiff and Motumal that instead of paying two annas share to Nindhi Bai for only one year and thereafter being at liberty to pay what he likes to her, he shall pay to her Rs. 200 per month from the date of the death of Kakumal up to such time as he carries on business in the premises aforesaid, namely, plots 101 and 111 N. P. 1, in the name of Hassomal Manghanmal or carries on business in the said premises in any other name, and so long as the said plaintiff is alive. If Motumal ceases to carry on business in the said premises but carries on business in other premises in the name of Hassomal Manghanmal during the lifetime of the plaintiff, this allowance will be reduced to Rs. 125 per month and shall cease on her death. If Motumal carries on business in the said premises up to the death of the plaintiff, then Motumal will give a sum of Rs. 5,000 (five thousand) in charity in memory of the plaintiff. If

Motumal has stopped carrying on business in the said premises during the lifetime of the plaintiff but he continued to carry on business in other premises in the name of Hassomal Manghanmal up to the time of the death of the plaintiff, then he shall pay Rs. 3,000 (three thousand) in charity. Such charity shall, however, be used for advancement of education. But it will be open to the plaintiff to leave testamentary directions as to the mode in which this money should be utilised provided it is not diverted from educational purposes. If Motumal ceases to carry on business in the said premises and also discontinues the name of Hassomal Manghanmal during the lifetime of the plaintiff, the allowance referred to above shall cease, and there shall be no obligation upon him to pay any money in charity. When defendant No. 1 (Motumal) gives up possession of the premises occupied by him, he will hand over possession thereof to the executors and trustees.'

3. In conformity with the agreement embodied therein Motumal continued during the accounting year 1939-40 to carry on business under the old name and style and in the old premises and paid to Bai Nindhi Bai the sum of Rs. 2,400 at the stipulated rate of Rs. 200 per month. The Income-tax Officer treated this sum as a revenue receipt negativing the assessee's contention that it was in the nature of a capital receipt, and computed the same as part of the assessable income of Bai Nindhi Bai. On appeal, the Appellate Assistant Commissioner affirmed that order. Bai Nindhi Bai preferred an appeal before the Tribunal and this Bench rejected the appeal holding that the said sum of Rs. 2,400 received by Bai Nindhi Bai from Seth Motumal is taxable income. The appellant has now applied for her case being stated to the Court contending that the following question of law arises from the order passed by this Bench in her appeal R. A. A. No. 5 (Sind) of 1941-42 :—

'Whether in the circumstances of this case the receipt of Rs. 2,400 by the appellant in consideration of the transfer of goodwill is rightly held by the Bench to be an income receipt in the appellant's hands ?'

The Commissioner of Income-tax, Bombay, Sind and Baluchistan, has filed a reply agreeing that the order passed by the Tribunal gives rise to a question of law, and proposing that the question be formulated in a slightly different form, *viz.*, :—

'Whether, in the circumstances of the case, the sum of Rs. 2,400 received by the assessee under the terms of the consent decree, dated the 21st November, 1935, has been rightly held to be taxable in her hands ?'

4. We are of the opinion that from the order of the Bench in the appeal a question of law arises and have consequently decided to refer the case to the Court.

5. On the facts set out above, the Tribunal held that having regard to the terms of the consent decree the real consideration for the acquisition

of these rights was not the relinquishment of her right to receive for a year a two annas share in the profits of the business but it was the appellant's consent to the use by Motumal of the goodwill of the business of Messrs. Hassomal Manghanmal. It was also found by the Tribunal that it was not a case of sale or out and out transfer of the goodwill for a determinate amount since it was open under the terms of the agreement embodied in the decree for Motumal to give up using the name and premises at any time he liked, and that in that case the goodwill would revert to the appellant. Motumal did not possess the right of further transferring the business name and premises. Alternatively, it was also found that even if it amounted to a case of out and out transfer of a capital asset the real object of the appellant was to secure an income for herself without the trouble and anxiety of herself working the capital asset, and not to receive the capital price of the goodwill.

6. On these findings the question of law that arises is :—

'Is the sum of Rs. 2,400 received by Bai Nindhi Bai from Seth Motumal in the year of account 1939-40 under the terms of the consent decree, dated the 21st November, 1935, taxable in the year of charge 1940-41 as the income of the appellant ?'

And we refer the same to the Chief Court of Sind under Section 66 (1) of the Income-tax Act."

Fatehchand Assudomal, for the assessee.

Partabrai D. Punwani, for the Commissioner.

JUDGMENT.

DAVIS, C. J.—This is a reference by the Commissioner of Income-tax, Bombay, Sind and Baluchistan, upon the following question :—

"Whether, in the circumstances of the case, the sum of Rs. 2,400 received by the assessee under the terms of the consent decree, dated the 21st of November, 1935, has been rightly held to be taxable in her hands."

The answer to that question, in our opinion, is in the affirmative.

The assessee in this case is one Bai Nindhi Bai, widow of one Seth Kakumal who, by his will, dated 13th April, 1932, bequeathed to his wife certain property, among which, it is alleged on behalf of the assessee, was the goodwill of a business carried on by this Kakumal Hassomal; and it is contended on behalf of the assessee that the monthly payments which the Income-tax Commissioner claims to be income in her hands are not income but merely capital payments spread out over a period of months in exchange for the goodwill of the business which, under the will of Kakumal, it is contended, belongs to her. It is, however, to be remembered that the payments which the assessee has received and which the Commissioner of Income-tax claims to be liable to taxation are not

made to her under the terms of the will but under the terms of the consent decree passed in a suit in which Bai Nindhi Bai had contested the validity of the will.

But it is helpful, in considering the consent decree, to consider the will which preceded it. In para. 7 of this will Kakumal bequeathed to his wife, Nindhi Bai, all the jewellery, ornaments, furniture and other things lying in his house absolutely including the cash, Rs. 26,000, then in her possession. He also left her residential houses and a plot of land described in this para. 7. And in para. 14 of his will he expressed his wish that on his death, Motumal his nephew, who was to carry on the business, should give Nindhi Bai a two annas share in the net profits of the business for twelve months and "thereafter as the said Motumal may think fit and proper, the said Motumal remaining *malik* of the shop business to be done in the name of my respected father Hassomal Manghanmal in whose name Shewaram Metharam traded all his life." At first sight it would appear that when Kakumal Hassomal provides under his will that his wife, Nindhi Bai, shall receive a two annas share out of the net profits of the shop business, he is providing not for capital payments but for payments out of the net profits of the business by way of income; and it is only by invoking the residuary clause, clause 17 of the will, that it can be alleged on behalf of the assessee that this two annas share of the net profits of the business is a capital payment.

It is alleged, on behalf of the assessee, that the sum of money now claimed to be liable to taxation was received in exchange for the goodwill of the business which Motumal is to carry on so long as he remains in the shop premises and the adjoining plots and carries on the business in the name of Hassomal Manghanmal, the respected father of Kakumal Hassomal. It is argued on behalf of the assessee that, under clause 8 of the will, plots 101 N.P. 1 and 111 N.P. 1 are not, under the will, devised to Motumal. They are to remain in his possession so long as he carries on the business and uses the prescribed name. When he ceases to do so, these plots and the goodwill of the business revert to Nindhi Bai.

So much then for the will. Now, in the consent decree in the suit brought by Nindhi Bai, clause 14 of the will is set out. Clause 14 of the will provides, as we have said, for a two annas share in the net profits of the shop business for twelve months and thereafter such payments as Motumal should think fit and proper. Instead, then, of this payment of a two annas share for twelve months and thereafter an uncertain sum dependent upon the goodwill of Motumal, it was provided in the compromise, clause 6, as follows:—

"It is agreed as between the plaintiff and Motumal that instead of paying two annas share to Nindhi Bai for only one year and thereafter being

at liberty to pay what he likes to her, he shall pay to her Rs. 200 a month from the date of the death of Kakumal up to such time as he carries on business in the premises aforesaid, namely, plots 101 and 111, N. P. 1, in the name of Hassomal Manghanmal or carries on business in the said premises in any other name and so long as the said plaintiff is alive. If Motumal ceases to carry on business in the said premises but carries on business in other premises in the name of Hassomal Manghanmal during the lifetime of the plaintiff, this allowance will be reduced to Rs. 125 per month and shall cease on her death."

Then the clause goes on to provide for the payment of certain sums to charity by Motumal on the death of Bai Nindhi Bai or should Motumal cease to carry on the business in the premises or to use the name of Hassomal Manghanmal.

We find it difficult to see how these money payments can be regarded as deferred payments of capital and not as income. Indeed, in clause 6 of the compromise, the payment is referred to as "the allowance" and this appears to us to be a case where the remarks of Courtney-Terrel, C. J., in *Commissioner of Income-tax* v. *Gopal Sharan Narain Singh*[1] are appropriate. The Chief Justice pointed out how the lady "has discarded the capital with its pleasures, burdens and risks and now enjoys an income only." This case of the Patna High Court was referred to with approval in a case of this Court reported in *Commissioner of Income-tax, Bombay Presidency, Sind and Baluchistan* v. *Mills Store Co., Karachi*[2].

Capital may be exchanged for capital: capital may be exchanged for income as in the case where a person buys an annuity and discards the pleasures, burdens and risks of capital for what is believed to be an assured income only. And we cannot say that either in the will or in the compromise it was contemplated that these payments to Bai Nindhi Bai should be regarded as capital payments being the sale price of the goodwill of the business; and, thus, it was contemplated that Bai Nindhi Bai, as a widow of Kakumal Hassomal, should share in the proceeds of the lucrative business which in his lifetime Kakumal had built up. It is alleged that the goodwill is exchanged for capital. Goodwill is an intangible asset, undoubtedly capable of valuation, but until it has been so valued we do not see how the question of capital at all arises. It cannot be said in this case that the alleged goodwill has been valued and has changed from an intangible to a tangible asset; and it is, we think, merely in the sphere of arguments that its conversion from an intangible to a tangible asset lies. As capital of one kind may be exchanged for capital of another kind, so an intangible asset can become a tangible asset or can be valued and become capital, but

(1) [1934] 2 I.T.R. 264. (2) [1941] 9 I.T.R. 642; I.L.R. [1941] Kar. 512.

neither in the will nor in the compromise does this appear to have been done. It appears to us that in the will Kakumal desired his wife should share in the proceeds of the business and that by the compromise this wish of Kakumal was made more certain of fulfilment with certain variations, respected and carried into effect.

In our view, then, the sum of Rs. 2,400 received by Bai Nindhi Bai is income, not capital; and as income liable to income-tax.

We think the Income-tax Commissioner is entitled to his costs. Order accordingly.

Reference answered accordingly.

[IN THE BOMBAY HIGH COURT.]

COMMISSIONER OF INCOME TAX, BOMBAY

v.

L. ARMSTRONG SMITH.

SIR LEONARD STONE, C.J., and KANIA, J. March 7, 1946.

INDIAN INCOME-TAX ACT (XI OF 1922), SECS. 7 & 12—COMPANY—ONE MAN COMPANY—CHAIRMAN AND MANAGING DIRECTOR—REMUNERATION RECEIVED UNDER ARTICLES FOR MANAGING COMPANY'S BUSINESS—WHETHER ASSESSABLE UNDER SEC. 7 OR 12.

A director of a company as such is not a servant of the company and the fees he receives are by way of gratuity. But that does not prevent a director or a managing director from entering into a contractual relationship with the company, so that, quite apart from his office of director he becomes entitled to remuneration as an employee of the company.

A business carried on by the assessee was taken over by a private limited company in which the assessee held most of the shares while two of his nominees held the rest. The Articles of Association of the company provided that the assessee was to be the Chairman and Managing Director of the company until he resigned office or died or ceased to hold at least one share in the capital of the company, that all the other directors were to be under his control and were bound to conform to his directions in regard to the company's business, and that his remuneration was to be voted by the company at its annual general meeting. The assessee devoted his whole time to the management of the company's affairs. He received a sum of Rs. 48,000 as his remuneration in the year of account:

Held, *that the remuneration of Rs. 48,000 received by the assessee was for managing the company's business and arose from his contractual relation with the company provided by the articles for performing the services of managing the company's business and that therefore his remuneration*

fell to be taxed under Section 7 and not under Section 12 of the Income-tax Act.

Bhagwati Shankar, In re [1944] (12 I.T.R. 193) *referred to.*

Reference under Section 66 (1) of the Indian Income-tax Act (XI of 1922) by the Income-tax Appellate Tribunal : (Income-tax Reference No. 12 of 1945).

STATEMENT OF CASE.

"The Commissioner of Income-tax, Bombay, Sind and Baluchistan, by his application, Exhibit A, requires us to state a case for the opinion of the High Court, Bombay, under Section 66 (1) of the Indian Income-tax Act, 1922, as amended in 1939. He has formulated two questions stated to be questions of law for their Lordships' opinion. The assessee by his written answer, Exhibit B, contends that no question of law arises.

2. The reference arises out of our judgment in the assessee's R.A.A. No. 286/Bombay of 1943-44 in connection with his assessment to income-tax for the financial year 1943-44.

3. The following is an agreed statement of facts. The assessee Mr. L. Armstrong Smith was carrying on a business as general merchant and commission agent till 18th June, 1941, when the business was taken over by a private limited company of Messrs. Armstrong Smith Limited. The company was incorporated under the Indian Companies Act (VII of 1913) on 24th June, 1941. Mr. Armstrong Smith holds most of the shares of the company while two of his nominees hold the rest. Under Article 58 of the Articles of Association of the company Mr. Armstrong Smith is the Chairman and Managing Director of the company. The article further provides that he shall remain the Chairman and Managing Director until he shall resign office or die or cease to hold at least one share in the capital of the company, and that so long as he retains the said office all other directors for the time being shall exercise such powers only as he may delegate to them and they shall be under his control and shall also be bound to conform to his directions in regard to the company's business. He devotes his whole time to the management of the company's affairs. Under Article 60 his remuneration is voted by the company at its annual general meeting. In the year of account material to the assessment for 1943-44 he received a sum of Rs. 48,000 as his remuneration in accordance with the resolution of the annual general meeting.

4. The Income-tax authorities brought the amount of remuneration to the tax under the head 'Income from other sources' under Section 12 of the Indian Income-tax Act repelling the assessee's contention that it was chargeable under the head of 'Salaries' under Section 7. The importance of the contention lay in the difference that the assessment under one or the other of the heads made to the amount of tax payable by the assessee.

Copies of the orders of the Income-tax Officer and the Appellate Assistant Commissioner are Exhibits C and D.

5. The assessee appealed to the Tribunal in R.A.A. No. 286. We held that the remuneration of Rs. 48,000 that the assessee received amounted to salary chargeable under Section 7 of the Act and not under Section 12. Our findings were that there was a relationship of an employer and an employee between the company and the assessee and that consequently the remuneration that he received in the year of account was chargeable as salary under Section 7 of the Act. Our reasons are recorded in paragraph 2 of our judgment, a copy of which is Exhibit E.

6. Dissatisfied with our finding the Commissioner has applied for reference. Ordinarily, the question whether a person is an employee of another is a question of fact. But in the present case it had to be decided with reference to the position that the assessee held under the general law and the Articles of Association. We think therefore that a point of law arises in this case. The Commissioner has formulated two questions which really speaking resolve into one and we submit it in the following form for their Lordships' opinion :—

Question referred.—Whether on the facts of the case the sum of Rs. 48,000 received by the assessee from Messrs. Armstrong Smith Ltd., is income from salary chargeable under Section 7 of the Indian Income-tax Act ? "

M. C. Setalvad, for the Commissioner.

Sir J. B. Kanga, for the assessee.

JUDGMENT.

STONE, C. J.—This is a reference under Section 66 (1) of the Income-tax Act. The question referred to us is:—

" Whether on the facts of the case the sum of Rs. 48,000 received by the assessee from Messrs. Armstrong Smith Ltd., is income from salary chargeable under Section 7 of the Indian Income-tax Act ? "

The assessment year in this case is the year 1943-44 and the accounting year is the calendar year 1943. There is no question but that this Rs. 48,000 is taxable; the only point is whether it falls to be taxed under Section 7 or under Section 12 of the Indian Income-tax Act.

From the agreed statement of facts, it appears that the assessee, Mr. L. Armstrong Smith, was carrying on a business as general merchant and commission agent till 18th June, 1941, when his business was taken over by a private limited company of Armstrong Smith Limited. The company was incorporated under the Indian Companies Act (VII of 1913) on 24th June, 1941. Mr. Armstrong Smith holds most of the shares of the company while two of his nominees hold the rest. Under Article 58 of the Articles of Association of the company Mr. Armstrong Smith is the

Chairman and Managing Director of the company. The article further provides that he shall remain the Chairman and Managing Director until he shall resign office or die or cease to hold at least one share in the capital of the company, and that so long as he retains the said office all other directors for the time being shall exercise such powers only as he may delegate to them and they shall be under his control and shall also be bound to conform to his directions in regard to the company's business.

Mr. Armstrong Smith devotes his whole time to the management of the company's affairs. Under Article 60 his remuneration is voted by the company at its annual general meeting. In the year of account material to the assessment he received a sum of Rs. 48,000 as his remuneration in accordance with the resolution of the annual general meeting.

Now, that being the statement of facts the Appellate Tribunal came to the conclusion that there was a relationship of employer and employee between the company and the assessee, and that consequently the remuneration that he received in the year of account was chargeable under Section 7 of the Act. The company is admittedly a legal entity, and it is a different legal entity from the assessee. The question is what is the legal relationship between the company and the assessee. It will be convenient at this stage to refer to the relevant sections of the Income-tax Act.

" Salaries ", which is the first head of the five heads of income set out in Section 6, is particularised and dealt with in Section 7 (1) which provides that the tax shall be payable by an assessee under the head " Salaries " in respect of any salary or wages, any annuity, pension or gratuity, and any fees, commissions, perquisites or profits in lieu of, or in addition to, any salary or wages, which are due to him from, whether paid or not by, a company. To that sub-section there are certain provisos which, as Mr. Setalvad on behalf of the Commissioner points out, import the idea of the assessee being subject to conditions of employment or conditions of service. Section 12, which has been described by the Privy Council as being the true residual section, provides that the tax shall be payable by an assessee under the head " Income from other sources " in respect of income, profits and gains of every kind which may be included in his total income (if not included under any of the preceding heads), and the rest of the section deals with allowances.

We have been referred to quite a number of English cases the effect of which can, I think, be summarised by saying that a director of a company as such is not a servant of the company and that the fees he receives are by way of gratuity, but that does not prevent a director or a managing director from entering into a contractual relationship with the company, so that, quite apart from his office of director he becomes entitled to remuneration as an employee of the company. Further that relationship may be created

either by a service agreement or by the articles themselves. Now, i case there is no question of any service agreement outside the article therefore, the relationship between the company and the assessee, Mr. S depends upon the articles. The group of articles which deal with dir commences with Article 57 which provides for the number of dire Article 58 is in these terms :—

" Leslie Armstrong Smith shall be Chairman and Managing Di of the company until he shall resign office or die or cease to hold at lea share in the capital of the company and so long as he shall retain th office shall have authority to exercise all the powers, authorities, and tion vested in the Directors by the Indian Companies Act, 1913, or articles and all the other Directors of the company for the time being exercise such powers only as he may delegate to them and they sh under his control and shall be bound to conform to his directions in to company's business."

Then Article 59 provides that two of the provisions in Arti which cause disqualification in a director and the articles with re the rotation of directors shall not apply to Mr. Smith. Under the h of "Powers and Duties of Directors" come Articles 64 and 65 wh as follows :—

" 64. The business of the company shall be managed by the Di who may exercise all such powers of the company as are not, by tl or any statutory modification thereof for the time being in force these articles, required to be exercised by the company in (Meeting, subject nevertheless to any regulation of these articles, provisions of the Act and to such regulations being not inconsiste the aforesaid regulations or provisions, as may be prescribed by th pany in General Meeting."

The rest of the article is not material. Then Article 65 :—

" The Directors may subject to the provisions of Article 58 fr to time appoint one or more of their number to the office of M Director or Manager for such term and at such remuneration (whe way of salary or commission or participation in profits or partly way and partly in another or others) as they may think fit and a so appointed shall not, while holding that office, be subject to re by rotation or taken into account in determining the rotation of re of Directors"

and then there is provision with regard to his appointment c he ceases to be a director of the company.

It is to be observed that Mr. Smith is under Article 58 appoi life and that there is vested in him the power to control and ma whole of the company's business and that so long as he retains

office no one else has any right to intervene in the management. In my opinion these articles fall under the head of creating a contractual relationship between the company and Mr. Smith by which Mr. Smith is to be in the service of the company. I do not think it is necessary to go through the English cases. The effect of them I have already stated, and a consideration of them leaves the matter in little doubt. There is only one Indian case on this subject and that is the case of *Bhagwati Shankar* [1]. In that case the assessee was an Advocate appointed by the High Court as official liquidator of a company at a salary which was fixed by the High Court at five per cent. on the assets actually realised by him, and it was held the commission earned by the assessee could be taxed only under Section 7 of the Income-tax Act. Mr. Justice Din Mohammad delivering the judgment with which Mr. Justice Marten agreed said this :—

"From the two sections of the Companies Act referred to above, three things emerge quite clearly : (1) that an official liquidator holds an office ; (2) that he is appointed by the Court ; (3) that he is to receive either a salary or a remuneration, by way of percentage or otherwise, as the Court may direct. In these circumstances Section 7 evidently applies to all commissions received by an official liquidator in the course of his employment. These commissions are in lieu of salary and can therefore neither be described as professional earnings so as to be covered by Section 11, nor can they be classified under 'other sources' so as to be governed by Section 12."

In my opinion, the remuneration of Rs. 48,000 received by the assessee is for managing this company's business, and arises from his contractual relationship with the company provided by the articles for performing the services of managing the company's business. In these circumstances his remuneration falls to be taxed under Section 7 and not Section 12, so that the question referred to us by the Tribunal should be answered in the affirmative. Commissioner to pay the costs.

KANIA, J.—I agree.

Reference answered in the affirmative.

[IN THE BOMBAY HIGH COURT.]

BRIHAN MAHARASHTRA SUGAR SYNDICATE LTD.

v.

COMMISSIONER OF INCOME TAX, BOMBAY.

SIR LEONARD STONE, C. J., and KANIA, J. April 8, 1946.

INDIAN INCOME-TAX ACT (XI OF 1922), SEC. 2 (1) (b) (iii)—AGRICULTURAL INCOME—INCOME DERIVED FROM SALE OF *Gul*—PROCESS OF CONVERTING SUGAR-CANE TO *Gul*—WHETHER NECESSARY TO RENDER THE

(1) [1944] 12 I.T.R. 193.

PRODUCE FIT FOR MARKET—QUESTIONS OF FACT AND LAW—FINDINGS OF TRIBUNAL—INTERFERENCE BY HIGH COURT.

The assessee company owned extensive areas of land on which sugar-cane was grown and also a sugar factory, and derived income from the sale of gul *manufactured in their factory. The Income-tax Tribunal found that the requirements of Section 2 (1) (b) (iii) of the Indian Income-tax Act were satisfied and that therefore the income in question was agricultural income:*

Held, *(1) that the question whether the requirements of Section 2 (1) (b) (iii) were made out was a question of law to be deduced from the facts, and the Court could go into that question though the question whether the conclusions of the Tribunal on pure questions of fact were justified, whether there was sufficient evidence to come to those conclusions, was not a matter for enquiry by the Court and on that point the Court had only to ask the question whether there was any evidence to justify the conclusion of fact;*

(2) that the conclusion of the Tribunal that the process employed by the assessee was a process ordinarily employed by a cultivator was one of fact and there was evidence to support it; but as there was a market for the sale of the sugar-cane before it was turned into gul, *the process employed was not a process ordinarily employed by a cultivator to render the produce fit to be taken to the market and the income derived from the sale of* gul *was not agricultural income.*

Cases referred to :—

Bomford *v.* Osborne ([1941] 2 A.E.R. 426; 110 L.J.K.B. 462; 165 L.T. 205; 57 T.L.R. 581; 10 I.T R. Suppl. 27).

Casey, J. M. *v.* Commissioner of Income-tax [1930] (4 I.T.C 259; 9 Pat. 185).

H. & S. Kinemas Ltd. *v.* Cooks [1933] (18 Tax Cas. 116).

Reference under Section 66 (1) of the Indian Income-tax Act (XI of 1922) by the Income-tax Appellate Tribunal: (Income-tax Reference No. 13 of 1943).

The facts are stated in the judgment.

Sir J. B. Kanga, for the assessee.

M. C. Setalvad, for the Commissioner.

JUDGMENT.

KANIA, J.—This is a reference under Section 66 (1) of the Indian Income-tax Act made by the Appellate Income-tax Tribunal. The question submitted for the Court's opinion is in these terms :—

"Whether in the circumstances of this case income derived by the assessee from sale of *gul* manufactured from sugar-cane is agricultural income within the meaning of Section 2 (1) (b) of the Income-tax Amendment Act, 1939, so as to be exempt from taxation under Section 4 (3) (viii) of the Act?"

The question arises in respect of the manufacture of *gul* by the assessee company, which is a joint stock company and has erected a sugar

factory. It owns large areas of land on which sugar-cane is grown. Section 2 (1) of the Income-tax Act defines agricultural income (omitting immaterial parts) as follows:—

" 'Agricultural income' means—

* * *

(b) any income derived from......land by

* * *

(ii) the performance by a cultivator......of any process ordinarily employed by a cultivator.........to render the produce raised......by him fit to be taken to market; or

(iii) the sale by a cultivator.........of the produce raised.........in respect of which no process has been performed other than a process of the nature described in sub-clause (ii)."

The rest of the section is immaterial. Although in the reference the Tribunal has referred to sub-clause (ii) it appears that the correct reference should be to Section 2 (1) (b) (iii) of the Act. The income in question is the result of sale of *gul* by the assessee company. It is not income derived by the performance of the process by the assessee as mentioned in sub-clause (ii). The material question still remains and is to be considered in two parts: (1) Whether the process is ordinarily employed by a cultivator and (2) Whether it is employed to render the produce raised by him fit to be taken to market.

When the matter was first submitted by the Tribunal for the Court's opinion the necessary facts from which the Court could say whether the two factors necessary to bring it in the definition were not found in the reference. We had therefore to refer the matter back to the Tribunal. The Tribunal has now made a further report in para. 3 of which they have set out the letter received by them from the Deputy Director of Agriculture. In para. 4 they have stated the extent of the area under sugar-cane cultivation in the Nira Canals Division. In para. 5 they have set out the report of the Inspector in respect of the process employed by the assessee in the manufacture of *gul*. Paragraph 6 contains a further report of the Inspector on the same point. In paragraphs 7 and 8 they have stated their conclusion on the materials before them. The relevant statements in paragraphs 7 and 8 are the following: (1) Use of machine power would not make any difference as regards the process employed. It may even be that machine power is more economical than bullocks if the production is on a larger scale. (2) The Inspector's report shows that the assessee company was not growing any soft quality of sugar-cane which could be sold for the purpose of chewing. (3) The sugar-cane grown by the assessee can either be sold to other sugar factory owners or utilised in the production of *gul* and sugar by the assessee company. (4) Some factory owners may require sugar-cane

for the production of sugar and purchase it from the small *bagaitdars*. (5) It may be possible for the small *bagaitdars* to sell the sugar-cane to the factory owners. (6) In the present case we do not think that the particular quality of sugar-cane which was used for the manufacture of *gul* could be sold by the assessee company. (7) We do not therefore think that the Inspector was right in assuming that the surplus of sugar-cane with the assessee company was marketable without being turned into *gul*, *i.e.*, saleable in its raw form. They conclude by stating that they were of the opinion that the requirements of the definition were made out. It may be noticed that throughout their statement of facts they have nowhere disbelieved any portion of the Inspector's report. The Inspector's report *inter alia* contains two statements which are material. The first is that the process employed by the assessee however differs from that of the agriculturists inasmuch as the company crushes the sugar-cane by means of crushers worked by an oil engine whereas the cultivators generally work the crushers by bullocks. In the further agreed statement of facts which the parties have put before us in paragraph 5 it is stated as follows: "These crushers and oil engine were used for crushing the sugar-cane and extracting juice therefrom and for boiling the juice." The second statement in the second report of the Inspector is this: "From these facts it can be said that the sugar-cane is marketable, without being turned into *gul*." A further statement although it appears to be hearsay is in these terms: "It is also reported that the *gul* manufactured by the assessee company is of the highest degree. It fetches more price as compared to the prices obtained by other manufacturers in the market. The company's *gul* is said to be of very good colour (*sic*) highest percentage of sugar as special chemicals are added by the company."

The first point discussed before us was whether having regard to the conclusion mentioned in the further statement of facts it is open to the Commissioner to contend that the requirements of the definition section have not been fulfilled. It was argued that the Tribunal being the final fact finding authority its statement that the process employed by the assessee was that ordinarily employed by the cultivator to render the produce raised by him fit to be taken to market is binding and the Department has no right to contend that the Court should go behind it. In this connection our attention was drawn to *H. & G. Kinemas Ltd.* v. *Cook*[1]. In that case the Commissioners had set out certain findings of the manner in which the new concern was being run by the assessees. Finlay, J. (as he then was), observed as follows: "I have come to the conclusion in this case that I cannot interfere with the decision of the Commissioners. I desire to say quite definitely that it is their decision and not mine. It is not necessary

(1) (1933) 18 Tax Cas. 116.

that I should express an opinion, and I do not express an opinion, as to whether, if I had been in their position, I should have arrived at the same conclusion." Our attention was also drawn to *Bomford* v. *Osborne*[1]. In that case the question for the Court's consideration was whether the assessee was liable to be taxed under rule 8 in respect of a certain area of land, because the profits were contended to arise from lands occupied as nursery and garden. From the facts it appears that the assessee was the occupier of 550 acres; 229 out of that were contended to be one holding. It was argued that because in a certain limited portion thereof some fruits were grown the area was liable to be assessed as garden land. The Commissioners recorded their findings in detail as to how the area of 229 acres was cultivated, what live stock remained on the farm, how labour and machinery was used, whether there was a separation of the garden area (so described) from the rest of the 229 acres and whether there was any demarcation of the areas. The conclusions were recorded in lettered paragraphs running from (a) to (r). The trial Court held that the conclusion that the whole area was garden land was correct and that was upheld on appeal, Scott, L. J., dissenting. When the matter came before the House of Lords it was contended that the conclusion that the profits of the things grown on the 229 acres were profits arising from land occupied as nursery and garden was not justified. Viscount Simon, L. C., in delivering judgment stated as follows: "No doubt there are many cases in which Commissioners, having had proved or admitted before them a series of facts, may deduce therefrom further conclusions which are themselves conclusions of pure fact. But in such cases the determination in point of law is that the facts proved or admitted *provide evidence to support* the Commissioners' conclusion." On behalf of the Commissioner it was urged before us that the Court has therefore jurisdiction to determine whether there was sufficient evidence for the conclusion of pure fact, as indicated by the Lord Chancellor in the above sentence. In my opinion this is not a correct reading of that judgment. The Lord Chancellor only meant, what has always been understood in matters of this kind to mean namely whether there was evidence on which the conclusion of fact recorded by the fact finding authority could be based. In the same case at page 36, Viscount Maugham stated as follows:—

"The question which emerges is *whether there are any facts* stated in the case which justify the course which the Commissioners took."

Similarly Lord Porter in the concluding part of his judgment stated as follows:—

"In the present case my view is that the splitting up of the holding for tax purpose was not justified and that there *was no evidence on* which the Commissioners could find that the portion which they so notional

(1) [1942] 10 I.T.R. Suppl. 27.

divided from the rest was occupied as a garden for the sale of produce." To emphasise the point I have italicized the words in the quoted paragraphs.

The question whether the requirements of the section are made out is a question of law to be deduced from the facts. The Court can go into that question. But the question whether the conclusions of the Tribunal on pure questions of fact are justified, whether there is sufficient evidence to come to those conclusions, is not a matter for inquiry by the Court. On that point the Court has only to ask the question whether there is any evidence to justify the conclusion of fact. That has been the consistent rule adopted by our Court and I find nothing in *Bomford* v. *Osborne*[1] to lead to a different conclusion. The close analysis of facts made by Lord Maugham is with a view to find out whether there was any evidence on which the conclusion of the Commissioners that the whole area was garden land could be justified. They were not considering the question whether the various pieces of evidence put together were sufficient to lead to that conclusion.

We have therefore to decide in this case whether the findings of fact recorded by the Tribunal are based on any evidence. As I have pointed out at the beginning, two ingredients are required to make the income agricultural in this case. The first point is whether the process employed by the assessee is ordinarily employed by a cultivator. I think there is evidence on which that conclusion is reached. The Tribunal accepted the report of the Inspector. The report shows that large cultivators use oil engine for crushing the sugar-cane, while small cultivators extract the juice by using the crushers worked by bullocks. It is further found that the process is substantially the same. There is therefore evidence that the process is ordinarily employed by a cultivator and the conclusion drawn from the facts is, in our opinion, to that extent, justified.

That however does not help the assessee. It has to be found that the process so employed is to render the produce fit to be taken to the market. In the present case the produce is sugar-cane. The article ultimately sold in the market, of which the profits are sought to be assessed, is not sugar-cane but *gul*. Reading the words used in the definition section with their natural meaning they must mean that the produce must retain its original character in spite of the process unless there is no market for selling it in that condition. If there is no market to sell the produce then any process which is ordinarily employed to render it fit to reach the market, where it can be sold, would be covered by the definition. In the present case the statement of case itself discloses that the sugar-cane grown by the assessee company can either be sold to other factories or utilised by the factory to produce *gul* or sugar. The Tribunal has further found that small cultivators sell their sugar-cane to factory owners. To put it in other words every

(1) [1942] 10 I.T.R. Suppl. 27.

owner of a sugar-cane factory manufacturing sugar or *gul* does not necessarily own sugar-cane fields. Conversely growers of sugar-cane, *i.e.*, farmers, do not necessarily own machinery which converts sugar-cane to *gul* or sugar. One important factor is noticed in the present case. It is stated that the sugar-cane grown by the assessee company is not fit for chewing. That however does not prevent there being a market in respect of this hard quality of sugar-cane. It only leads to the conclusion that a particular section of humanity cannot use this variety of sugar-cane in its natural form. But there is a large section of people to whom this variety is useful. They buy and sell the same. If so, within the meaning of the definition section, there is a market for this commodity. This construction of the word "market" is supported by *J. M. Casey* v. *Commissioner of Income-tax*[1]. In that case the assessee prepared sisal fibre for sale in market by means of machinery, from aloe plants cultivated by him. It was found that there was no cultivation of aloe plants save in connection with the economic process involving the use of machinery such as was employed by the assessee, barring the laborious and uneconomic process employed by the jail authorities. It was held that under the circumstances there was no market, in the proper sense of the word, for the aloe leaves. It was argued on behalf of the Commissioner that the raw aloe leaves had a market. That was negatived because it was found as a fact that raw aloe leaves by themselves would not be sold. The argument that the only process ordinarily employed by the cultivator to render the article fit for being taken to market in the case of aloe leaves after being cut was decortication (*i.e.*, extraction of fibre), was rejected. After reviewing the evidence which was put before the Court it was observed in the concluding part of the judgment as follows :—

"The conclusion at which I arrive is that if a generalisation may be made from the single instance available, then the process ordinarily employed by the cultivator of the aloe plant in order to render his produce fit to be taken to market is that in fact employed by the assessee and the whole of the profits derived by him from the manufacture of sisal fibre is agricultural income...It may be that in the future the economic conditions may change. If the growth of the aloe leaf should become established as an agricultural industry by itself, and if the manufacturers of sisal fibre cease to cultivate the plant themselves and should purchase the leaves in an open market, then such circumstances may possibly require reconsideration in the light of the income-tax law......"

Our observations in this case are limited to the facts noticed in the reference. I have already pointed out that the report of the Inspector, which is not disbelieved, shows that the sugar-cane grown by the assessee is marketable without being turned into *gul*. The Tribunal in the first part

(1) (1929) 4 I.T.C. 259.

of paragraph 7 (finding No. 3) has recorded that the sugar-cane grown by the assessee can either be sold to other factory owners or utilised in the production of *gul* etc. If so, there is a market where this sugar-cane can be sold without passing through any process. We therefore think that the Tribunal was in error in overlooking this fact, because on their own statement there is evidence to show that the produce, which in this case consists of sugar-cane, requires no process to be employed to make it fit to be taken to market.

The result is that the question submitted for our opinion must be answered in the negative. The assessee to pay the costs of the reference throughout.

Reference answered in the negative.

[IN THE BOMBAY HIGH COURT.]

POONA ELECTRIC SUPPLY CO., LTD.

v.

COMMISSIONER OF INCOME TAX.

KANIA and CHAGLA, JJ. March 23, 1945.

INDIAN INCOME-TAX ACT (XI OF 1922), SEC. 10 (2) (vi)—DEPRECIATION—ELECTRIC SUPPLY COMPANY—CHANGE FROM D. C. TO A. C. SYSTEM—DEPRECIATION ON EXPENDITURE INCURRED FOR REPLACEMENT OF CONSUMERS' FANS, RADIOS, ETC.—WHETHER ALLOWABLE.

The assessees, an electric supply company, started converting the supply of electrical energy from D. C. to A. C. system and were obliged under the provisions of the Indian Electricity Act and under the terms of their licence to change and substitute at their own cost the consumers' equipments such as fans, radios, etc., so as to enable such equipments to be worked on A. C. system. In doing so they had to make alterations in their own cables, service lines and meters and replace consumers' fans, radios, etc. The expenditure incurred was conceded by the assessees to be capital expenditure but they claimed depreciation in respect of such expenditure. The Income-tax Appellate Tribunal allowed depreciation in respect of expenditure incurred for alteration of the company's cables and lines but rejected the claim for depreciation in respect of expenditure incurred for replacement of consumers' fans, radios, etc.

Held, *that depreciation could not be allowed in respect of the expenditure incurred for replacement of consumers' fans, radios, etc., inasmuch as under Section 10 (2) (vi) of the Income-tax Act depreciation could be allowed only in respect of the property of the assessee.*

Nagpur Electric Light and Power Co., Ltd. v. *Commissioner of Income-tax, C. P. and Berar* [1932] (6 I. T. C. 303) *referred to.*

Reference under Section 66 (1) of the Indian Income-tax Act (XI of 1922) by the Income-tax Appellate Tribunal: (Income-tax Reference No. 24 of 1944).

STATEMENT OF CASE.

"These four applications by the assessee under Section 66 (1) of the Indian Income-tax Act relate to four successive assessments and arise out of the orders of the Tribunal in R.A.A. Nos. 93 to 96 (Bombay) of 1943-44. As the facts are the same and the issue involved is identical, this statement of the case and the question formulated herein will cover all the four applications.

2. The assessee company started converting supply of electrical energy from D. C. to A. C. and in doing so, the company was obliged under the provisions of the Indian Electricity Act and under the terms of its licence to change over and substitute at its cost, consumers' equipment, such as fans, radios, etc., so as to enable the consumers' equipment to be worked on the A. C. system. When the direct current (D. C.) supply is changed to alternating current (A. C.), material changes have to be made not only with regard to consumers' apparatus but also in the distribution system and in respect of the services and meters. The assessee claimed the entire expense incurred in the course of conversion during the four accounting years under review as revenue expenditure; in the alternative, depreciation in respect of the same was claimed under Section 10 (2) (vi) of the Act. The Income-tax Officer negatived both the claims. The assessee appealed to the Appellate Assistant Commissioner, who while upholding the Income-tax Officer's view as to the expenditure being of a capital nature held that depreciation on such capital expenditure was due to the company and allowed the same.

3. The Income-tax Officer preferred four appeals to the Tribunal in respect of the assessments for 1939-40, 1940-41, 1941-42 and 1942-43. The Tribunal found:—

(a) following *Nagpur Electric Light and Power Co., Ltd.* v. *Commissioner of Income-tax, Central Provinces and Berar*[1], that the expenditure was of a capital nature;

(b) on the admission of the counsel for the Department that the assessee company is entitled to depreciation allowance in respect of the expenditure incurred in relation to the distribution system and the services; and

(c) that the distribution system ends with the plugs and thereafter the rest of the apparatus is the property of the consumer, that no part of

(1) (1932) 6 I.T.C. 303.

it was at any time intended to be or treated as an asset of the company and that consequently the assessee company is not entitled to claim depreciation on the cost of changing that portion of the plant which in fact belonged to the consumers and did not belong to the assessee.

The Income-tax Officer was directed to make the necessary apportionment between the expenditure on the company's assets and the expenditure on the consumers' assets and to give proportionate relief to the assessee. The total sums expended on conversion during the respective years of account, the bulk of which was admittedly spent on consumers' assets, have been correctly set out in the assessee's application for reference.

4. The assessee claims that out of the findings adverted to in paragraphs 2 and 3 (c) above, a question of law arises which he desires to be referred to the High Court. The Commissioner in reply agrees that a question of law arises for reference to the High Court but objects to the alternative question propounded by the assessee.

5. We are of the opinion that a question of law arises from the orders of the Tribunal in the four appeals referred to previously and would formulate the question as below so as to cover all the four assessments under reference and refer the same to the High Court of Judicature at Bombay under Section 66 (1) of the Indian Income-tax Act :—

"Is the assessee company entitled to depreciation allowance under Section 10 (2) (vi) of the Income-tax Act for the assessment years 1939-40, 1940-41, 1941-42 and 1942-43 on the cost of the replacement or alterations of that portion of the apparatus which belonged to the consumers and was not the property of the company."

Sir J. B. Kanga, for the assessee.

M. C. Setalvad and *G. N. Joshi*, for the Commissioner.

JUDGMENT.

KANIA, J.—This is a reference made by the Tribunal of Appeal under Section 66 (1) of the Income-tax Act. The relevant facts, which are found in the statement of case, are these :—

The assessee company started converting the supply of electric energy from D.C. to A.C. system and they were obliged under the provisions of the Indian Electricity Act and under the terms of their licence to change and substitute at their own cost the consumers' equipment such as fans, radios, etc., so as to enable the consumers' equipment to be worked on A.C. system. In doing so, they had to make alterations in their own cables, service lines and meters. They claimed the entire expenses incurred in the course of conversion during the four accounting years, as revenue expenditure. That claim was rejected. Having regard to the decision in *Nagpur Electric Light and Power Co., Ltd.* v. *Commissioner of Income-tax* [1] the point was

(1) (1932) 6 I.T.C. 303.

not pressed before the Tribunal. The Income-tax Officer had negatived both the claims but the Appellate Assistant Commissioner, while upholding the Income-tax Officer's view about the expenditure being of capital nature, held that depreciation on such expenditure was due to the company and allowed the same. The taxing authorities being dissatisfied with the decision, preferred an appeal to the Tribunal. Before the Tribunal the question whether this expenditure was of capital nature or revenue expenditure was not argued. It was accepted as capital expenditure. The only contention urged before the Tribunal was that, this being capital expenditure, the company had expended the whole money in changing over from D.C. to A.C. system and just as expenditure in respect of alterations of the company's cables and lines was capital expenditure, the replacement cost of the consumers' fans, radios etc., was also a part of the capital expenditure of the company. Following that line of reasoning it was urged that as depreciation was allowed in respect of company's cables etc., depreciation should also be allowed in respect of cost of replacement of fans, radios etc., as the two stood on the same footing. This argument had appealed to the Appellate Assistant Commissioner but was rejected by the Tribunal. The Tribunal permitted depreciation in respect of company's properties, but rejected the claim for depreciation in respect of the expenditure incurred for replacement of fans, radios etc., although it held that the expenditure was of capital nature.

It was urged on behalf of the assessees that all this expenditure was for alteration of the system of the company and as depreciation was permitted in respect of the one part of the expenditure it should also be permitted in respect of the other part. In our view this argument overlooks the express words of Section 10 (2) (vi) of the Act. That clause provides for an allowance in respect of depreciation of such buildings, machinery, plant, or furniture, being the property of the assessee, a sum equivalent to such percentage on the written down value as may in any case or class of cases be prescribed. The clause therefore clearly applies only to the property of the assessee ; it illustrates the property as being buildings, machinery, plant or furniture ; it provides for a written down value thereof on a certain percentage basis which may be fixed by the rules. The section therefore clearly contemplates, as is ordinarily understood, the depreciation in value of the assessee's own assets. The argument of the assessees is that the costs incurred in replacing the consumers' fans, radios etc., are also costs incurred in respect of company's property, because without that expense the company's system will not work. It was contended that as the company is allowed to debit to capital expenditure, the cost of repairs or replacement of the pavement when a cable is replaced, and as depreciation is allowed in respect of such expenses, depreciation should be

allowed also in respect of the cost of replacement in the present case. This argument overlooks the fact that the expenses incurred in replacing the pavement are in respect of the cable which is placed by the company. It is directly connected with a tangible asset of the company. In our opinion, therefore, that analogy is not proper. It should again be borne in mind that in respect of every expenditure of capital nature the Income-tax Act does not permit depreciation. It is only in respect of the property of the assessee, that provision is made for depreciation. If this expenditure, although it is of capital nature, is not considered expenditure in respect of the assessees' property, no depreciation can be permitted. As the expenditure is in respect of the property of the consumers, although it is incurred for working the system of the company, it is still an expenditure not in respect of the property of the assessees. Therefore the case is not covered by Section 10 (2) (vi) and in our opinion the conclusion of the Tribunal is correct. The question referred to us is limited to depreciation and it does not raise the question whether this expenditure is of capital nature or a revenue expenditure. Confining our answer to the question submitted to us, the answer must be in the negative. The assessees to pay the costs of the reference.

Reference answered accordingly.

[IN THE BOMBAY HIGH COURT.]

COMMISSIONER OF INCOME TAX

v.

POONA ELECTRIC SUPPLY CO., LTD.

KANIA and CHAGLA, JJ. March 27, 1945.

INDIAN INCOME-TAX ACT (XI OF 1922), SEC. 10 (2) (vi) & (5)—INCOME OR CAPITAL—DEPRECIATION OF MACHINERY—ACTUAL COST, MEANING OF—ELECTRIC SUPPLY COMPANY—CONTRIBUTIONS RECEIVED FROM GOVERNMENT FOR CONSTRUCTING NEW SUPPLY LINES—WHETHER INCOME OR CAPITAL—WHETHER FORM PART OF ACTUAL COST TO ASSESSEE.

The assessee, an electric supply company, undertook to supply electricity to the Government in certain areas on condition that it was allowed to charge Government the cost of materials and labour charges plus fifteen per cent. for supervision for the complete work. The assessee received in the accounting year contributions amounting to Rs. 36,310 from the Government. These contributions were non-refundable and were made towards, and represented only a part of, the capital cost of constructing the new supply lines, which works were regarded by the assessee as unremunerative and would not have been undertaken without the contributions in question :

Held, (*i*) *that the contributions amounting to Rs. 36,310 were not trading receipts but were capital receipts and as such were not assessable to tax in the hands of the assessee;*

(*ii*) *that the contributions formed part of "the actual cost to the assessee" within the meaning of Section 10 (5) of the Income-tax Act.*

In determining the question what is the actual cost of a machinery or plant to the assessee, it is an irrelevant consideration whether the assessee has spent the whole amount or only a part of it. What the taxing authorities have to consider is what the actual cost of the article is independently of who has contributed towards that particular amount.

Corporation of Birmingham v. *Barnes* ([1935] A.C. 292; 104 L.J.K.B. 281; 152 L.T. 558; 19 Tax Cas. 195; 3 I.T.R. (Eng. Cas.) 26) *applied.*

Reference under Section 66 (1) of the Indian Income-tax Act (XI of 1922) by the Income-tax, Appellate Tribunal, Bombay: (Income-tax Reference No. 29 of 1944).

STATEMENT OF CASE.

" These two applications are by the Commissioner of Income-tax, Bombay, under Section 66 (1) of the Income-tax Act to refer to the High Court certain questions of law arising out of the orders of the Tribunal in R. A. A. Nos. 94 and 69-Bombay of 1943-44. Both the applications are concerned with the same item, *viz.*, contributions made by Government to the assessee company. The question raised in one application is whether the said contributions constituted trade receipts of the company and were taxable as such, while the question involved in the other application is whether, if they are deemed to be a capital receipt, they form part of the actual cost to the assessee for the purpose of calculating the depreciation allowable upon such cost under Section 10 (2) (vi) of the Income-tax Act. The two applications are therefore consolidated and dealt with together.

2. During the accounting period ended December 31, 1941, relating to the charge year 1942-43 the miscellaneous earnings of the assessee company amounted to Rs. 52,812-9-8, out of which a sum of Rs. 36,310 represented the contributions paid by consumers for extensions of the mains. The entire sum of Rs. 36,310 was in this instance paid by one consumer only, namely, the Government. The contributions were non-refundable and were made towards, and represented only a part of, the capital cost of constructing certain new supply lines, which works were regarded by the company as unremunerative and would not have been undertaken without the contributions in question. The contributions were thus admittedly made in respect of a capital expenditure and for the purpose of helping the company to meet its expenditure in constructing the additional lines of supply required; they were given for the purpose of adding to and completing the capital sum required for doing the work. The receipts were

ultimately utilised towards the expenditure on a capital asset and the expenditure was debited to the asset account of the company. After the contribution, works are executed by the company, the ownership of the new supply lines vests in the company, and the company is obliged to maintain, and from time to time to replace, the supply lines.

3. The receipts from such contributions, when realised, were being credited by the company to the revenue account and were being shown under the head "Revenue from mains extensions," and they had in previous years been assessed to tax as the "miscellaneous earnings" of the company. In the assessment year under reference, however, it was contended by the assessee company before the Income-tax Officer that the contributions were in the nature of a capital receipt and as such should not be included in the assessable profits of the company. The Income-tax Officer rejected the plea but on appeal by the assessee, the Appellate Assistant Commissioner took a different view and held that the contributions were capital receipts in the hands of the company and hence not liable to assessment. The Income-tax Officer appealed to the Tribunal against the aforementioned order of the Appellate Assistant Commissioner. In its order in R.A.A. No. 94-Bombay of 1943-44 the Tribunal agreeing with the Appellate Assistant Commissioner's view, affirmed his order. It was found by the Tribunal that the contributions were made by the Government for the purpose of enabling the company to execute the capital scheme of extending the mains, or in other words, in order to advance a capital expenditure to be made by the company, and that the said contributions were received by the company not as part of their profits or gains or as a sum which went to make up the profits or gains of their trade. The Tribunal was satisfied with the explanation furnished by the assessee for crediting the contributions to "miscellaneous receipts" in the company's accounts and was further of the opinion that the method of accounting would not *per se* alter the true character of the sums received.

4. In paragraph 5 of the application in 66 R. A. No. 56-Bombay of 1943-44 a position, which seems somewhat different, has been developed, *viz.*, "that the contributions were in fact a part of the price paid by the consumer in order to secure a supply of electricity in a particular area for a limited period. Instead of charging increased rates for the electricity supply, as would otherwise have been necessary, the company demanded an advance payment which would enable it to charge the ordinary rates without incurring a loss on the undertaking as a whole." At the assessment stage and before the Appellate Assistant Commissioner as well as before the Tribunal the contention at best was, to put it in the words of the Appellate Assistant Commissioner, that "being regularly earned by the company from year to year in the normal course of the company's business, they (the contributions) are really extra or additional charges recovered

from them over and above the schedule rates fixed for the supply of the current by the company to consumers." The Appellate Assistant Commissioner discountenanced the argument and held that the contributions were made "obviously with a view to help the company because the company was not in a position financially to undertake such extensions unless some such contributions from Government were forthcoming. In short they were contributions towards capital cost." The Tribunal, on a close scrutiny of the facts and circumstances of the case, accepted this view of the Appellate Assistant Commissioner and adopted the reasons furnished by him. The theory of 'advance payment' adumbrated in the application was not presented at an earlier stage and hence was not the subject of enquiry by the Tribunal. Being essentially a matter of fact, it cannot, we apprehend, be raised at the present stage.

5. The Commissioner and the assessee agree that on the findings recorded by the Tribunal a referable question arises. We are of the opinion that a question of law arises out of the order of the Tribunal, and would formulate the same as in paragraph 9 (a) below.

6. If this question is answered in the affirmative, the reference in 66 R. A. No. 55-Bombay of 1943-44 will not require to be considered, as the question raised therein is based on the assumption that the aforementioned contributions are capital receipts and not trading profits.

7. In the appellate order of the Appellate Assistant Commissioner referred to in paragraphs 3 and 4 *supra*, while holding that the contributions must be treated as on capital account, the Appellate Assistant Commissioner directed that the sum of Rs. 36,310 "should be adjusted against the capital expenditure incurred, so that for the purpose of the depreciation allowance on the mains the capital cost would be the cost incurred by the company less the contributions received from the Government." The company appealed to the Tribunal against this part of the Appellate Assistant Commissioner's order and by its order in R. A. A. No. 69/Bombay of 1943-44 the Tribunal held that even though a portion of the capital cost of extending the mains or of constructing new lines of supply was provided by the consumer and was not met by the company from its own resources, the total expenditure incurred in constructing the new supply lines constituted the "actual cost to the assessee," within the meaning of that expression in Section 10 (5) and it was consequently directed that the sum of Rs. 36,310 should be left altogether out of account (*i.e.*, should not be taken into consideration at all) in ascertaining the actual cost of the new extensions for the purpose of calculating the depreciation allowance admissible under Section 10 (2) (vi) of the Income-tax Act. For the necessary findings of fact in connection with this part of the case reference will also be necessary to the order of the Tribunal in R. A. A. No. 94/Bombay of

1943-44, since the orders in the two connected appeals have, for all practical purposes, to be treated as one order (*vide* also paragraph 2 *supra*).

8. With regard to this matter also both the Commissioner and the assessee agree that a question of law arises out of the findings of the Tribunal. We are of the same view.

9. Under Section 66 (1) of the Income-tax Act we refer the following questions to the High Court of Judicature at Bombay :—

(*a*) Whether on the facts found by the Tribunal the contributions amounting to Rs. 36,310 received by the assessee company from Government during the accounting period are trading receipts and are, as such assessable to tax in the hands of the company.

(*b*) If the contributions are in the nature of capital receipts, do they form part of 'the actual cost to the assessee' within the meaning of Section 10 (5) of the Income-tax Act."

M. C. Setalvad and *G. N. Joshi*, for the Commissioner.

Sir J. B. Kanga, for the assessee.

JUDGMENT.

CHAGLA, J.—Two questions have been raised in this reference: (1) Whether on the facts found by the Tribunal the contributions amounting to Rs. 36,310 received by the assessee company from Government during the accounting period are trading receipts and are, as such assessable to tax in the hands of the company.

The contention of the company is that these receipts are not trading receipts but capital receipts being contribution towards capital expenditure made by the consumers which in this case happen to be Government. The position is this: On 5th December, 1940, the Chief Engineer, Southern Command, wrote to the company requesting the company to let him know the estimate of the cost for giving service in the areas mentioned in the letter. On 10th December the company replied that the price of materials would vary from time to time and therefore it was not possible for them to give a firm quotation but they were prepared to charge Government the cost of materials and labour charges plus fifteen per cent. for supervision for the complete work. In pursuance of this correspondence the company undertook the work of supplying electricity to the areas to which it had not supplied it before and for that purpose it had to construct new supply lines and in respect of those lines Government paid a sum which is in question, *viz.*, Rs. 36,310. Mr. Setalvad contends that this is a part of the company's remuneration and therefore chargeable as the profit and income of the company. It is clear that the company would not have constructed these new lines and given the supply of electricity to Government unless they received Government contribution towards capital expenditure to be incurred by the company in laying down these new lines. This contribution

is not in the nature of recurring income or receipt. It is not as if the company is charging Government anything more for supplying electricity to them but what the company tells Government is: "we are not in a position, and we do not propose, to incur capital expenditure to supply electricity to you unless you contribute towards the same." When Government agreed to make this contribution the company agreed to incur capital expenditure to supply electricity to Government. In our opinion therefore the first question raised must be answered in the negative. They are not trading receipts: they are capital receipts.

The other question raised is:—

If the contributions are in the nature of capital receipts, do they form part of "the actual cost to the assessee" within the meaning of Section 10 (5) of the Income-tax Act.

Now, under Section 10 (2) one of the permissible deductions is in respect of depreciation of a certain percentage of the written down value as may in any case or class of cases be prescribed. "Written down value" is defined in Section 10 (5) (a) as, in the case of assets acquired before the previous year, the actual cost to the assessee. The question that arises is, what is the actual cost to the assessee. Does the expression "actual cost" mean only what the assessee is out of pocket by, or does the expression mean only the costs the whole costs and nothing but the costs to use the words of Lord Atkin in the judgment to which I shall presently refer. The House of Lords were considering the rule in the English Income-tax Statute which deals with the question of depreciation. The decision is reported in *Corporation of Birmingham* v. *Barnes*[1]. The scheme of depreciation under the English Act is slightly different from the scheme under our Act. The English Act considers what the wear and tear of a particular machinery or building is in the course of the year. The Commissioner determines the wear and tear and permits depreciation but the subsequent rule provides that in no event the aggregate of the depreciation to be allowed by the Commissioner should exceed the actual cost to the assessee of the machinery or the particular article being depreciated and in construing the "actual cost to the assessee" the House of Lords came to the conclusion that what was to be considered was what the actual cost of making the article or machinery was independently of who had contributed towards that particular amount. It was entirely an irrelevant consideration whether the assessee had spent the whole amount or only a part of it. What the taxing authorities were concerned with was what the actual cost of the article was. Therefore in our opinion it is not permissible to exclude from what constituted the actual cost to the assessee the sum of Rs. 36,310. Therefore, the answer to the second question will be in the affirmative.

The Commissioner to pay the costs of the reference.

Reference answered accordingly.

(1) (1935) 19 Tax Cas. 195; 3 I.T.R. (Eng. Cas.) 26.

[IN THE BOMBAY HIGH COURT.]

NATIVE SHARE AND STOCK BROKERS' ASSOCIATION

v.

COMMISSIONER OF INCOME TAX.

SIR LEONARD STONE, C.J., and KANIA, J. October 13, 1944.

INDIAN INCOME-TAX ACT (XI OF 1922), SEC. 10 (6)—TRADE ASSOCIATION —STOCK EXCHANGE—SCHEME FOR EMPLOYMENT AND CONTROL OF AUTHORISED CLERKS BY MEMBERS—ANNUAL ADMISSION FEES—WHETHER ASSESSABLE INCOME—" REMUNERATION FOR SPECIFIC SERVICES."

The rules of a stock brokers' association (the Bombay Stock Exchange) provided a definite scheme for allowing members to employ authorised clerks and for the admission, registration, conduct, control and supervision of the authorised clerks for the benefit primarily of the members who employed them and received from the members an annual fee of Rs. 100 for the admission of each authorised clerk: Held, *that the income received by the association by way of fees was remuneration definitely related to specific services performed by the association for its members within the meaning of Section 10 (6) of the Indian Income-tax Act and was assessable to income-tax.*

Reference under Section 66 (1) of the Indian Income-tax Act (XI of 1922) by the Income-tax Appellate Tribunal: (Income-tax Reference No. 15 of 1944).

STATEMENT OF CASE.

"Under Section 66 (1) of the Indian Income-tax Act, 1922, we are submitting this reference to their Lordships of the High Court of Bombay at the instance of the assessee, the Native Share and Stock Brokers' Association, whose application in this connection is marked Exhibit A in the annexure. The Commissioner of Income-tax, Bombay, Sind and Baluchistan, has filed a written answer, Exhibit B.

2. The reference relates to an assessment made upon the assessee for the charge year 1940-41. A copy of the assessment order made by the Income-tax Officer is Exhibit C. The assessee took the assessment in successive appeals to the Appellate Assistant Commissioner and the Appellate Tribunal. Copies of the appellate orders are Exhibits D and E.

3. The question that we propose to submit for their Lordships' opinion arises out of facts which are stated in paras. 2 and 3 of our judgment. Briefly speaking, the assessee Association is a mutual concern recognised by the Government of Bombay under the Bombay Securities Contracts Control Act (VIII of 1925), and its purpose is to assist and control

the business of buying, selling and dealing in stocks, shares and securities. It has framed rules with the sanction of the Government. One of its objects set out in rule 2 is to support and protect the character and status of brokers, to further the interests of both brokers and the public dealing in Bombay in stocks, shares and securities, to promote honourable practices, to settle disputes among brokers and decide all questions of usage, custom or courtesy in conducting brokerage business. A broker on his being elected to membership has to pay an annual subscription, besides entrance fee. On payment he is entitled to exercise the rights and privileges of a member some of which are admission to the market, clearing and settling contracts through the Clearing House and a right to participate in the governance of the Association. It is common ground that the receipts of the Association from the entrance fees and membership subscriptions are not chargeable to income-tax. According to the rules, a member alone is entitled to be admitted to the market and the Clearing House and he alone can enter into and settle transactions with other members. Also no non-member can be admitted to the trading ring or the Clearing House for settling contracts. Rules 47 to 58 provide for the employment of a limited number of authorised clerks by the members. A member desirous of obtaining admission to the market for his authorised clerk has to apply for permission to the Governing Board in a prescribed form. On such permission being granted the authorised clerk is entitled to admission to the market and to transact business on behalf of his employer, and a member is liable for all the bargains made by such clerk with other members. An authorised clerk is admitted to the market during his good behaviour and the Board has absolute discretion to refuse admission or suspend or terminate the right of admission without assigning any reason. Under the rules a member has to pay to the Association an annual subscription of Rs. 100 or such fee as may be prescribed from time to time, in respect of each authorised clerk appointed by him. It is also admitted that a member has to pay a similar subscription in respect of a sub-broker that may be appointed by him.

In the year of account material to the present assessment the Association's receipts from the authorised clerks and sub-brokers' fees just described aggregated to Rs. 1,22,600. The Income-tax authorities included this amount in the computation of the assessee's taxable income.

4. It was contended before us that the authorised clerks and sub-brokers' fees or subscriptions, like the membership fees, were not taxable being receipts of a mutual concern. Under Section 10 (6) of the Act, a trade, professional or similar association performing specific services for its members for remuneration definitely related to those services is deemed, for the purpose of Section 10, to carry on business in respect of those

services, and the profits and gains therefrom are liable to tax accordingly. On a consideration of this provision and the facts we rejected the assessee's contention and held that the amount of Rs. 1,22,600 was rightly considered in the computation of the assessee's taxable income under Section 10 of the Act. Our reasons are recorded in para. 5 of our judgment.

5. Being dissatisfied with our decision the assessee has invited us to refer the point of law to the High Court and has formulated two questions in that connection. But we agree with the Commissioner in thinking that only one question arises for reference and we submit it in the following form :—

Question referred.—Whether the sum of Rs. 1,22,600 received by the assessee Association in respect of authorised clerks and sub-brokers' fees or subscriptions in the year of account is remuneration definitely related to specific services performed by the Association for its members, within the meaning of sub-section (6) of Section 10 of the Indian Income-tax Act, 1939?"

Sir J. B. Kanga, for the assessee.
M. C. Setalvad, for the Commissioner.

JUDGMENT.

STONE, C. J.—This is a reference under Section 66 (1) of the Income-tax Act. The assessee is the Native Share and Stock Brokers' Association of Bombay more commonly known as the Bombay Stock Exchange. The Association is recognised by the Government under the Bombay Securities Contracts Control Act, 1925, and there are rules made by the Association for the regulation and control of transactions in securities, so that it becomes what is referred to in the Act as a "recognised Stock Exchange." Being a mutual association not formed for the purpose of making profits it does not pay income-tax unless its activities come within Section 10 (6) which is as follows :—

"A trade, professional or similar association performing specific services for its members for remuneration definitely related to those services shall be deemed for the purpose of this section to carry on business in respect of those services, and the profits and gains therefrom shall be liable to tax accordingly."

The question referred to us concerns the assessment year 1940-41 or the accounting year, which is the calendar year 1939. The question submitted is :—

"Whether the sum of Rs. 1,22,600 received by the assessee Association in respect of authorised clerks and sub-brokers' fees or subscriptions in the year of account is remuneration definitely related to specific services

performed by the Association for its members, within the meaning of sub-section (6) of Section 10 of the Indian Income-tax Act, 1939?"

The sum of Rs. 1,22,600 represents 1,226 fees or subscriptions of Rs. 100 each paid in respect of the authorisation by the Association of 1,226 clerks or remisiers belonging to some 475 firms which admit them to certain privileges or rights in the exchange building which otherwise they could not enjoy under the rules of the Association. The short question is whether the Association is performing specific services for its members for remuneration definitely related to these services.

Sir Jamshedji Kanga on behalf of the Association says that the sum of Rs. 100 is the licence fee paid by a member for the granting of the facilities which the member would not otherwise enjoy and this is not performing services by the Association who grants the licence. The facility granted is merely admission of clerks and remisiers of the members to the exchange building and that no services are performed by the Association for its members. In the alternative he says that if any services are performed they are performed for all the members and not only for those members who pay the fees of Rs. 100 and that therefore the remuneration does not definitely relate to any services rendered to the member paying them. On the other hand, Mr. Setalvad on behalf of the Commissioner submits that the answer is to be found by asking the question, "for the remuneration paid, what, if any, are the services performed?" He draws our attention to some of the rules which he says show a definite scheme for the admission and supervision of the authorised clerks and which confer definite advantages to the members who pay the fees. Turning to the rules the relevant group of rules commences with rule 47, which is headed, "Authorised Clerks" and is as follows:—

"47. (a) The Board shall from time to time fix the number of authorised clerks a member may be allowed to employ.

(b) Members of the Association may be employed as authori clerks in excess of the number permitted by this rule. A member so employed shall not himself be entitled to employ any authorised clerk.

(c) A member may with the permission of the Board employ his remisier also as his authorised clerk but not in addition to the number of authorised clerks allowed to him under this rule."

Turning for a moment to rule 172 (1) it will there be found that it implements sub-rule (c) because it is as follows:—

"172. (1) A remisier shall be entitled to admission to the market on payment of an annual fee of Rs. 100 in advance or such higher fee as may be prescribed from time to time by the Board and shall wear a distinctive badge; but he shall not make bargains in his own name or on behalf of his employer."

Now sub-rule (d) of rule 47 provides as follows :—

"47. (d) A member desirous of obtaining admission to the market for his authorised clerks shall apply for the permission of the Board in such form as the said Board may from time to time prescribe."

This actual form has been produced and in effect and in substance it is a notification that the member intends to employ certain person as his authorised clerk and on the back of the form are certain undertakings signed by the clerk.

Sub-rule (e) is as follows :—

"(e) The employer shall pay to the Association an annual subscription of Rs. 100 or such higher fee as may be prescribed from time to time in respect of each authorised clerk employed by him. No such subscription shall be payable in respect of a member who acts as an authorised clerk."

This is the background of the scheme.

The next rule in chronological order which is relevant for the present reference is rule 50 (a) and is as under :—

"50. (a) The Secretary of the Association shall keep a register for authorised clerks and shall enter in such register the name of the clerk and of the member who employs him, the dates of the beginning and termination of his employment or the withdrawal of his authorisation."

Then comes rule 53 which provides as follows :—

"53. (a) A member and his authorised clerk when in the market must wear a badge. No clerk without such badge shall be admitted into the market to transact business."

Rule 48 (a) provides for admission in the market in the following terms, *viz.*, "An authorised clerk is entitled to admission in the market and no clerk who is not authorised is so entitled." That is followed by rule 49 which provides what an authorised clerk may do, and is as under :—

"49. (a) An authorised clerk or a member acting as an authorised clerk shall transact business only on behalf of his employer. He shall not make bargains in his own name or in the name of any other than that of his employer or sign contracts in his own name or in any other name or on behalf of his employer, unless he holds a power of attorney for the purpose as provided in rule 167 (d).

(b) The Board shall expel immediately an authorised clerk or a member acting as an authorised clerk who contravenes this rule."

Then we come to the important rule 52 which is the good behaviour rule and it provides that :—

"Authorised clerks shall be admitted to the market only during good behaviour and the Board may by a resolution in their absolute discretion refuse admission to the market to the authorised clerk of any member and

may at any time suspend or terminate the right of admission of such clerk without assigning any reason whatsoever."

Finally we come to rule 50 (b) which provides for the termination of the employment of the authorised clerks and is as follows :—

"A member employing an authorised clerk or terminating the employment or withdrawing the authorisation of such clerk shall give notice in writing to the said Secretary of the name of such clerk and of the date of the beginning or termination of his employment or the withdrawal of his authorisation and the said Secretary shall forthwith post the notice of such employment, termination or withdrawal upon the notice board of the Association."

In my judgment these rules lay down a definite scheme and provide an organised arrangement, controlled and supervised by the Association for the benefit of its members. In my opinion the carrying of their scheme into effect is performing services for its members by the Association. No doubt the benefit of the scheme would redound to the benefit of all members since all would have the advantage of disciplined supervision exercised over the authorised clerks and remisiers of the others. I do not think that because the payment for the carrying of the scheme is provided for only by members who avail themselves of the use of the authorised clerks it makes any difference. It cannot make a difference whether the remuneration for the services performed is provided by some or all the members provided it is supplied by members. In my opinion the services performed are specific because they provide an identifiable scheme laid down with sufficient clarity and in my opinion the remuneration is definitely related to the services and is for the benefit of the members of the Association. Accordingly in my opinion the answer to the question referred to the Court should be in the affirmative.

KANIA, J.—I agree. The relevant sections of the Act and the material rules of the Association have been set out in the judgment of the learned Chief Justice. Under Section 10 (6) of the Act the question to be considered is whether this Association is performing specific services for its members, and, if so, whether the remuneration in question is definitely related to those services. If the answer to these two questions is in the affirmative the assessee becomes a person carrying on business in respect of those services and becomes liable to tax accordingly. For its ordinary activities this Association not being formed for the purpose of making profits is not taxed because it does not carry on business. Section 10 (6) is an exception in respect of associations of this kind. Broadly speaking, the object is that although the Association may not ordinarily be carrying on business, if for a stated remuneration it renders specific services to its members, it is admitted

to be carrying on business for that portion of its activities and is liable to be taxed accordingly. In order to answer the two questions which I have formulated at the commencement it is therefore necessary to examine the rules and determine whether by reason of those rules the Association is performing specific services for its members. A perusal of the rules referred to in the judgment of the learned Chief Justice shows that the institution of authorised clerks exists for the benefit only of those who pay remuneration of Rs. 100 instead of going to the market and carrying on their business themselves. Individual members are permitted to work through an agent. For that the charge is made. The rules provide for the application and grant for such permission, registration of the authorised clerks on the individuals being recognised as clerks of particular members, supervision over the work of such clerks and particularly to prevent them from registering contracts either in their own name or in the name of another member; and a general supervision over their good behaviour is contemplated. Moreover on a clerk ceasing to be a clerk of the individual member proper entries have to be made in the register. This is in order to prevent a member who had employed such authorised clerk being liable thereafter for the transactions effected by such clerks. It is clear that the scheme taken as a whole is based on the institution of the authorised clerks and their work for the members who employ them. For that the Association has to render services which I have briefly described above. Those are clearly specific services rendered by the Association for its members who desire to employ authorised clerks.

It was argued on behalf of the assessee that these are facilities given to the members and not the performance of specific services by the Association. That contention overlooks the fact that the Association has undertaken certain obligations by the rules towards its members in accepting these fees. By the rules the Board and the Secretary have to perform certain duties as prescribed by the rules in respect of authorised clerks. It is therefore futile to contend that they amount merely to facilities and do not constitute performance of services by the Association.

A question was raised as to whether these are specific services to be performed for particular members or whether the rules amount to performance of duties towards members in general. It is true that several of the services to be rendered may be helpful to the other members for their business. Taken as a whole I consider that as a performance of services by the Association for the benefit of members who pay the remuneration. But for the institution of authorised clerks such services would not come into being at all. The rules are primarily framed to show what agent is employed by what member and up to what date. The general supervision is also in respect of the individual acts of the authorised clerk in respect of the

transactions of his principal who had employed him. It seems therefore that the specific services to be performed by the Association are in respect of the members who pay the fees.

The second question is whether the remuneration is definitely related to these services. The answer to this again also depends on the construction of the rules. On the payment of Rs. 100 " the authorised clerk " comes into existence. All the services which the Association has thereafter to render are in respect of the authorised clerk who has thus come into being. It is therefore clear that the remuneration paid brings into existence the authorised clerk in respect of whom the specific services are definitely related. In my opinion therefore the two requisites of the section are fulfilled under the rules of the Association and the conclusion of the Tribunal is correct. I therefore agree that the answer to the question submitted to us should be in the affirmative.

The assessee to pay the costs of the reference.

Reference answered in the affirmative.

[IN THE BOMBAY HIGH COURT.]

N. V. KHANDVALA v. COMMISSIONER OF INCOME-TAX.

SIR LEONARD STONE, C. J., and KANIA, J. March 12, 1946.

INDIAN INCOME-TAX ACT (XI OF 1922), SEC. 66—REFERENCE—STATEMENT OF CASE IN PURSUANCE OF HIGH COURT'S ORDER—APPLICATION TO DIRECT TRIBUNAL TO RAISE FURTHER QUESTIONS OF LAW—PROPER STAGE FOR HEARING APPLICATION—SCOPE OF SEC. 66.

When a statement of case, with the question of law framed by the Tribunal, is filed in Court for disposal, if a party is aggrieved and wants to contend that certain further facts ought to be stated, or certain questions of law should be raised, he can make an application by way of notice of motion. That should be heard along with the case stated by the Tribunal for the Court's opinion.

On an application by the assessees under Section 66 of the Income-tax Act the Bombay High Court directed the Income-tax Appellate Tribunal to state a case. According to the practice of the High Court, the questions of law were not formulated by the Court, but were left to be raised by the Tribunal. The Tribunal prepared a case and submitted for the Court's opinion one question of law. The assessees were dissatisfied with the action of the Tribunal and filed a petition praying for an order directing the Tribunal to state for the Court's opinion four more questions of law:

Held, *that the proper time for the assessees to bring to the notice of the Court that certain further and other facts were necessary to be stated or certain further or other questions of law arose was at the hearing of the case stated by the Tribunal.*

Income-tax Application No. 3 of 1945.

Sir Jamshedji Kanga, for the petitioners.

M. C. Setalvad, for the Commissioner.

JUDGMENT.

KANIA, J.—This rule is taken out by the petitioners inviting the Court to raise four questions of law mentioned in the rule.

The assessees are stock-brokers. They were assessed for Samvat year 1993 (November 15, 1936, to November 3, 1937) by the Income-tax Officer on their total estimated income and ordered to pay Rs. 16,07,622 under Section 23 (4) of the Indian Income-tax Act. The amount was reduced on appeal to the Tribunal by about four lakhs. It was pointed out before the Income-tax Officer that the books of account kept by the assessees were not reliable. It was further contended that the method of accounting adopted by the assessees did not correctly show their profits and income, and therefore under the proviso to Section 13 of the Income-tax Act the computation had to be made upon such basis and in such manner as the Income-tax Officer might determine. The assessees contended that this did not entitle the Income-tax Officer to adopt any unjust or arbitrary method. The assessees applied to the Tribunal to state a case for the opinion of the Court, but that application was rejected. The assessees thereupon took out a notice of motion for an order asking the Tribunal to state a case. That was disposed of on July 26, 1944, when a Bench of this Court directed the Tribunal to state a case. According to the practice of our Court the questions of law were not formulated by the Court. They were left to be raised by the Tribunal.

Acting upon that judgment, the Tribunal has prepared a case and submitted for the Court's opinion one question of law. The assessees are dissatisfied with that action of the Tribunal. This petition was therefore filed by the assessees praying for an order that the Tribunal do state for the Court's opinion four more questions of law. Those questions are set out in detail in the rule which the assessees obtained on the petition. A preliminary objection is raised on behalf of the Commissioner. It is contended that before the case stated by the Tribunal is brought before the Court for disposal, it is not open either to the assessee or the Commissioner to ask the Court to call upon the Tribunal to state either further facts or raise further questions of law. It is argued that when the statement of case is before the Court for disposal, if the Court finds that proper questions on the case have

not been raised, the Court may formulate the questions and dispose them of. It is not disputed that if the questions of law submitted for the Court's opinion require a further statement of facts from the referring authority, the Court has power to call for such further statement under Section 66 (4) of the Indian Income-tax Act. The objection is to an attempt to obtain an order before the statement of case and the question of law raised by the Tribunal are before the Court for disposal. The objection is to the stage at which an application should be made by the aggrieved party. For the present discussion it makes no difference whether the aggrieved party is the assessee or the Commissioner.

Having read in detail Section 66 of the Indian Income-tax Act, it appears to us that the objection of the Commissioner is proper. It is not right to allow parties to rush to Court and invite it to ask the Tribunal to send a further statement of facts, or to submit a question of law, before the Court has an opportunity to consider the case actually submitted by the Tribunal for its consideration. It seems to us that the most convenient way to deal with the situation is this. When a statement of case, with the question of law framed by the Tribunal, is filed in Court for disposal, if a party is aggrieved and wants to contend that certain further facts ought to be stated, or certain questions of law should be raised, he can make an application by way of notice of motion. That should be heard along with the case stated by the Tribunal for the Court's opinion. At that time the Court will consider whether the statement of case is complete for the question of law raised by the Tribunal. The Court can also consider whether on the case stated by the Tribunal the proper question is raised or not. That is the proper time for an aggrieved party to bring to the notice of the Court that certain further and other facts are necessary to be stated or certain further or other questions of law arise and should be brought for decision by the Court.

As this is the first case in which this argument is advanced and the Court is invited to express its opinion on the procedure, we direct that the present rule do stand over to the hearing of the case stated by the Tribunal in pursuance of the order made by the Court on July 26, 1944. Costs of this hearing will be costs in the reference.

Ordered accordingly.

[IN THE BOMBAY HIGH COURT.]

METRO THEATRE BOMBAY LTD.

v.

COMMISSIONER OF INCOME-TAX.

SIR LEONARD STONE, C. J., and KANIA, J. November 9, 1944.

INDIAN INCOME-TAX ACT (XI OF 1922), SECS. 9 (1) (iv), 10 (2) (iii), 10 (2) (xii)—BUILDING AGREEMENT—CINEMA THEATRE—FIXED SUM PAYABLE TO GRANTOR OF LAND IN INSTALMENTS WITH INTEREST ON OUTSTANDING INSTALMENTS—BUILDING PARTLY LET OUT AND PARTLY USED AS CINEMA—INTEREST ON INSTALMENTS—WHETHER ALLOWABLE AS INTEREST ON BORROWED CAPITAL, AS INTEREST ON CHARGE OR AS BUSINESS EXPENDITURE.

The assessee entered into a building agreement with the Government by which in consideration of building upon the land and paying a sum of three lacs and odd rupees it was to receive a lease for 999 years. The agreement provided for the payment of this sum in six-monthly instalments with interest on the instalments outstanding from time to time. The assessee claimed deduction of a sum of Rs. 9,825 which was payable as interest under this agreement in the relevant year. The building was partly used as a cinema and partly let out to others. There was a provision in the agreement that if the assessee made default in the payment of any instalment it would be lawful for the Government to recover the same under the Bombay City Land Revenue Act after notice of demand thereunder in the same manner as if the same were an arrear of land revenue due in respect of the said land :

Held, (*1*) *that the interest claimed in respect of the portion let out for rent could not be allowed under Section 9* (*1*) (*iv*) *of the Indian Income-tax Act as interest on a charge on the land inasmuch as a charge does not arise under Sections 10 and 13 of the Bombay City Land Revenue Act unless and until there has been a default and a notice has been issued ;* (*2*) *that the interest claimed in respect of the portion used for cinema was not allowable as interest on borrowed capital under Section 10* (*2*) (*iii*) *as there was really no borrowing of capital, nor as business expenditure under Section 10* (*2*) (*xii*) *as the amount in question was not spent wholly and exclusively for the purposes of the business.* Per KANIA, J.—*As there was no question of the passing of ownership until all the instalments were paid, the question of a charge under the Transfer of Property Act did not arise. For the same reason the interest could not be considered to have been paid in respect of the property "acquired" within the last portion of Section 9* (*1*) (*iv*) *of the Act.*

A mere purchase of capital asset on a long term credit with a stipulation for the payment of interest on the reduced balance does not

amount to the borrowing of capital within the meaning of Section 10 (2) (iii).

Cases referred to :—

Hudson Bay Co. *v.* Thew [1919] (7 Tax Cas. 206; [1919] 2 K.B. 632; 121 L.T. 385; 35 T.L.R. 683).

Secretary of State *v.* Sir Andrew Scoble ([1903] A.C. 299; 72 L.J.K.B. 617; 51 W.R. 675; 4 Tax Cas. 618).

Reference under Section 66 (1) of the Indian Income-tax Act (XI of 1922) by the Income-tax Appellate Tribunal: (Income-tax Reference No. 22 of 1944).

STATEMENT OF CASE.

"This is an application by Metro Theatre Bombay Ltd., requiring the Tribunal to state a question of law, arising out of the Tribunal's order in R. A. A. No. 153 (Bombay) of 1943-44, to the High Court of judicature at Bombay.

2. During the assessment proceedings for 1942-43, the assessee claimed a deduction of Rs. 9,825 under Sections 10 (2) (iii) and 9 (1) (iv) of the Income-tax Act, representing partly the amount of interest paid in respect of capital borrowed for the purposes of the business and partly the interest paid on capital borrowed for the purposes of acquiring property. The Income-tax Officer disallowed the claim under both the heads on the ground that the expenditure in dispute represented capital expenditure. On appeal the Appellate Assistant Commissioner agreed with the view taken by the Income-tax Officer and rejected the appellant's claim. An appeal was then preferred to the Tribunal which was determined by the Tribunal's order above referred to. The facts, as found by the Tribunal, are that the assessee leased a plot of land from the Secretary of State for a period of 999 years. The lease agreement is dated 24th June, 1937. The total premium was fixed at Rs. 3,81,796 and the Government agreed to accept payments in half-yearly instalments of Rs. 19,090 to be spread over a period of 20 years, plus interest at 5 per cent. on the reducing balance. The assessee erected a building upon the leased land. A part of this building is used as a cinema house and a part of it is let out on hire. During the year of account, the applicant paid, under the terms of the lease, a sum of Rs. 9,825 by way of interest. An allocation has been made of this sum into the amount properly chargeable to the business and the amount relating to the interest paid on capital borrowed for the acquisition of property. It was argued before the Tribunal that the arrangement with the Government was tantamount to borrowing a sum of money from the Government at fixed interest rate; but the Tribunal repelled this contention and concluded that Sections 10 (2) (iii) and 9 (1) (iv) of the Income-tax Act speak of capital borrowed and the process of reasoning adopted

on behalf of the assessee did not bring the transaction within the meaning of the above-mentioned provisions. The Tribunal was of the opinion that the payment of interest on the reducing balance did not amount to payment of interest on borrowed capital. In this view, the Tribunal rejected the balance claimed.

3. In this application the applicant has formulated a question of law, which is agreed to by the Commissioner and which appears to us to bring out precisely the point involved. The following question is, therefore, referred to the High Court of Judicature at Bombay under Section 66 (1) of the Income-tax Act:—

'Whether the said sum of Rs. 9,825 or any portion thereof is a permissible deduction in arriving at the total assessable income of the assessee.'"

F. J. Coltman, for the assessee.

M. C. Setalvad, for the Commissioner.

JUDGMENT.

STONE, C. J.—This is a reference under Section 66 of the Indian Income-tax Act in respect of an assessment order for the year 1942-43 and the sum in dispute is Rs. 9,825 which the appellant claims to be a deduction. The matter arises in this way. The appellant entered into a building agreement with the Government by which in consideration of building upon the land and paying a sum of three lacs and odd rupees it was to receive a lease for 999 years. The agreement provides for the payment of the amount by six-monthly instalments with interest on the instalments outstanding from time to time. It is in respect of Rs. 9,825 which was the interest payable in the relevant year that the reference is made. It is agreed by both the parties that the sum of Rs. 9,825 has in fact to be split in two sums, since it is in respect of the building which has now been built upon the land and which is used partly as a cinema in the occupation of the appellant and partly let out to others for rent, so that the total sum is made up of two sums of Rs. 1,361 in respect of the portion let out which is assessable to tax under Section 9 under the heading "Income from property" and Rs. 8,464 in respect of the cinema which is assessable under Section 10 under the heading "Profits and gains from business, profession or vocation." Now before turning to the two sections and permissible deductions which may be made thereunder it is necessary to say something about the building agreement which is dated 24th June, 1937. It is between the Governor-General of India in Council of the one part and the appellant of the other part. It first of all recites that "whereas the licensee (*i.e.*, the appellant) has offered to purchase from the grantor (the Governor-General) a lease for 999 years of the piece of land described in the first Schedule hereto for the sum of Rs. 3,81,796 on the terms and conditions hereinafter contained........" Then there is a recital with regard to a deposit

and a further recital that the appellant had agreed to pay the purchase money by instalments of Rs. 19,090 as therein mentioned. Then comes the operative part of the agreement, clause 1 of which is as follows :—

"In consideration of the premises and of the licensee agreeing to pay the sum of Rs. 3,81,796 to the grantor by instalments with interest as hereinafter mentioned and on the conditions and agreements hereinafter contained on the part of the licensee to be observed and performed, the grantor grants to the licensee licence and authority only to enter upon the piece of land described in the first Schedule hereunder written and delineated on the plan annexed hereto and thereon surrounded with a red line for the purpose of building and executing works thereon as hereinafter mentioned and for no other purpose whatever and until the grant of such lease as is hereinafter mentioned the licensee shall be deemed to be a bare licensee only of the premises but subject to the terms of the lease as if it had actually been executed in so far as the same is applicable to these presents."

Then the paragraph goes on to provide for a power of revocation :—

"...........provided the grantor shall have given to the licensee ninety days previous notice of his intention so to do specifying the default complained of and provided the licensee shall not have remedied such default within such period and upon the revocation thereof the licensee shall have three months from the date of revocation in which to vacate the premises and remove its property...."

Clause 2 provides for the conditions which the licensee has to observe and perform and the first condition is to pay to the grantor the purchase money and the instalments. The periods during which they are to be paid, including the amount of the first deposit, are there set out. That clause contains the following relevant and important proviso :—

"...........provided always that if the licensee shall make default in the payment of any instalment on the days when the same are payable it shall be lawful for the grantor without prejudice to his other rights and remedies to recover the same under the Bombay City Land Revenue Act (II of 1876) as amended and after notice of demand thereunder in the same manner as if the same were an arrear of land revenue due in respect of the said land."

Clause 3 provides for a certificate of completion in these terms :—

"As soon as the grantor has certified that all buildings have been erected in accordance with the terms hereof and provided that the licensee shall have paid all sums payable under these presents and shall have observed all the stipulations and conditions hereinafter contained the grantor will grant and the licensee or its approved nominee (if any) will accept a lease......of the said land and its building erected thereon for the term of 999 years from the date hereof at the yearly rent of rupee one (if demanded)..........."

The agreement contains a number of other provisions such as are usually found in such agreements. Schedule II contains the building rules and finally in Schedule III the form of lease, which was ultimately to be granted when the lessee had performed the conditions which he had covenanted to observe and perform, is set out.

That being the agreement to which the appellant is a party and under which he holds the land and building, a part of which is let out, it is now necessary to look at the exemptions or deductions to the two relevant sections of the Income-tax Act.

Section 9 is the section which deals with that head of income called "Income from property," and taxes chargeable under it are subject to certain allowances. Sub-section 9 (1) (iv) is as follows:—

"Where the property is subject to a mortgage or other capital charge, the amount of any interest on such mortgage or charge (is exempted)."

It is therefore necessary to consider whether this property is subject to a capital charge. Mr. Coltman on behalf of the appellant submits that because of the proviso in clause 2 of the building agreement the provisions of the Bombay City Land Revenue Act, 1876, are applicable and he points out that under Section 10 of that Act "the arrears of land revenue due on account of land shall, on failure by the persons interested therein to pay the same within the date specified in that behalf in a notice demanding payment posted on or near the land, be a permanent charge on the land and every part thereof." Section 13 of that Act is also relied on. That section gives power to collect arrears of land revenue in default of payment by attachment and sale. Mr. Setalvad's answer on behalf of the respondent is that there is no charge as it does not arise unless and until, not only has there been a default but also a certain notice has been given. Turning again to the relevant paragraph in the building agreement it is to be observed that the proviso is that if the lessee shall make default in the payment of any instalment on the dates when the same are payable the respondent is given the right, without prejudice to his other rights and remedies to recover the same, to proceed to recover the same under the Land Revenue Act. So that before Section 10 of that Act can operate and make the arrears a permanent charge there has not only got to be a default but there has got to be a notice served pursuant to the agreement. That being so there is no existing charge at the present time and therefore no capital charge within the meaning of Section 9 (1) (iv) of the Indian Income-tax Act.

It is now necessary to consider the other sum of Rs. 8,464 in respect of that portion of the building which is now in the occupation of the appellant and upon which he carries on the cinema business. Section 10 deals with profits and gains of business, profession or vocation and it

provides that such profits and gains shall be computed after making certain allowances. Now there are various heads of these allowances and two of them are relied upon by Mr. Coltman. The first is contained in sub-section (2), clause (iii), which reads as follows :—"In respect of capital borrowed for the purposes of the business, profession or vocation, the amount of the interest paid (is exempted)." Dealing with this question the Appellate Tribunal in its judgment has stated :—

" The analogy of this transaction to a borrowing pure and simple may sound plausible but in interpreting a taxing statute one cannot go merely on analogies when the language of the relevant enactment bears a plain and unambiguous meaning. What Section 10 (2) (iii) speaks of is interest on capital borrowed for the purpose of business. A mere purchase of capital asset on a long term credit with a stipulation for the payment of interest on the reduced balance does not, in our opinion, amount to the borrowing of capital within the meaning of Section 10 (2) (iii)." I agree with the passage quoted above and the short answer to Mr. Coltman's argument is that when the building agreement is analysed it is found that no capital is borrowed by it.

The other head is under sub-section (2) (xii) and the allowance made by it is this: " Any expenditure (not being in the nature of capital expenditure or the personal expenses of the assessee) laid out or expended wholly and exclusively for the purpose of such business, profession or vocation (is exempted)." In my judgment this interest payment on unpaid instalments cannot be stated to be wholly or exclusively a payment for the purpose of such business. No doubt the payment of interest on the arrears of purchase price of this leasehold interest in which the business is carried on may be said to be for the purposes of the business but it is not wholly or exclusively for the purposes of the business. For example, if the cinema business had to be closed down the appellant would still have to make this payment unless he was prepared to have the licence forfeited. For that reason I do not think the sum of Rs. 8,464 falls within clause (xii) of sub-section (2).

The result is that the question submitted to us by the Tribunal must be answered in the negative. The assessee to pay the costs of the reference.

KANIA, J.—The relevant portions of the Income-tax Act and the agreement under which the assessee obtained the premises to erect the building and acquired the right to obtain the lease have been set out in the judgment of the learned Chief Justice.

The question referred to us involves a sum of Rs. 9,825 which the assessee paid by way of interest on the balance of the premium payable under the agreement, in the accounting year. The building is partly let

out and partly used for the business of the assessee. The result is that in his assessment in respect of the income of this building, the assessment is made partly under Section 9 and partly under Section 10. Having regard to the terms of the agreement, in respect of the income allocated to his business, he claims exemption for payment of interest under Section 10 (2) (iii). Before the Income-tax authorities and the Tribunal the claim was made only under that sub-section. Before us a further additional ground was urged and Mr. Coltman claimed that the exemption was covered by Section 10 (2) (xii) also. In respect of his income from property he claimed exemption under Section 9 (1) (iv) on the ground that the property was subject to a capital charge and the amount of interest was paid on the amount of such charge. In the alternative he claimed exemption under the last sentence of the same sub-clause, *viz.*, that the amount of interest was payable on the capital by the use of which the property has been acquired. Rs. 8,464 are allocated in respect of his business income while Rs. 1,361 are allocated in respect of his property income out of this interest payment.

I shall first consider the claim to exemption under Section 10 (2) (iii) Mr. Coltman claimed that the transaction amounted to payment of interest on the capital borrowed for the purposes of business. It was urged that the Court need not look only at the words used in the agreement. He relied on *Secretary of State* v. *Sir Andrew Scoble*[1] in support of the contention that the Court should look at the real nature of the transaction. That proposition is not disputed. A scrutiny of the agreement shows that till the lease was obtained the assessee is only a licensee. He has agreed to purchase this property on payment of a sum of Rs. 3,81,796. He is given some facility in payment of the same by instalments as provided in clause 2. It is recognized that the obligation is to pay the whole amount and therefore for the facility granted for deferred payments interest has to be paid by the assessee in respect of the balance which remained unpaid. The minimum amount of instalment is also stipulated, but the assessee has the right, if he so chooses, to pay a larger amount and reduce his liability to that extent, both for payment of the price and the payment of interest. I am unable to accept the contention of the assessee that the transaction amounts to capital borrowed for the purposes of the business. The transaction is not a loan transaction, secondly it is not for the purposes of business. It was argued that the assessee could have gone to a bank, borrowed the money and paid off the grantor the amount due under the agreement and in that event he would have been entitled to claim deduction in respect of the interest paid. The short answer to this contention is that it has not been so done. I should not be understood as accepting that argument even if a loan was so taken, because I am not sure that

(1) [1903] A. C. 299.

the loan would be considered as taken for the purposes of the business. On the materials before us it is not shown that the purpose of the business of the assessee is to acquire immovable properties. That aspect of the case is not before us and I do not pronounce any opinion on that aspect. On the construction of the agreement it is clear that no loan of any amount was taken from the grantor and the interest was not paid on such capital borrowed for the purpose of the business.

The alternative ground of exemption under Section 10 (2) (*xii*), as I have pointed out, was not argued before the Tribunal. Fundamentally it is a question of fact because it has first to be ascertained that the expenditure was wholly and exclusively for the purposes of business. On the footing that certain facts are found on which there is a conclusion that the expenditure was wholly or exclusively for the purposes of such business, and that conclusion being an inference would be a question of law, we have permitted counsel to urge this argument. On that point also the assessee cannot get the exemption claimed. The business is of showing cinema films. That business can be conducted in rented premises and it cannot be argued that this amount was the payment of rent. In *Hudson Bay Co.* v. *Thew*[1], an argument was advanced that the payment was in the nature of rent but was rejected. This payment again can in no event be stated to be an expenditure "wholly or exclusively for the purposes of business." If the interest was not paid the result would be not necessarily the stoppage of the business of showing cinema films, but the assessee will not acquire the lease of this property. It is therefore clear that this new ground urged by Mr. Coltman does not help the assessee.

The ground for exemption claimed under Section 9 can be sustained only if the assessee shows that the property is subject to a capital charge and the interest is paid on such capital charge. This argument is based on the contention firstly that on a true construction of clause 2 of the agreement, because the grantor has a right to resort to remedies to recover unpaid instalments after notice of demand in the same manner as if the same were an arrear of land revenue under the Bombay City Land Revenue Act, the instalments are a charge on the land in question, and interest is paid in respect of the said charge. In my opinion this whole contention is founded on an assumption which does not exist. The right of the grantor to esort to remedies under Act II of 1876 arises only on default of payment of any instalment. On the facts on record it is common ground that there has occurred no default in payment of any instalment. Therefore no occasion has arisen to resort to the remedies to recover the said instalments. Reading Sections 10 and 13 of the Land Revenue Code it is clear that in order to bring into existence the paramount charge contemplated by Section 10 two conditions are necessary: (1) omission to pay the land

(1) (1919) 7 Tax Cas. 206.

revenue by the time it has become due, and (2) affixing of a notice in or about the property as mentioned in the second paragraph of that section. A perusal of Section 13 shows that the notice required under Section 10 is altogether of a different nature from the notice required to be served under Section 13. The notice under the last mentioned section has to be served on the person liable to pay the land revenue primarily. On default, the Collector is entitled to proceed to sell the land. When proceedings are adopted under Section 13 only, no question of a paramount charge arises. If the Collector desires to secure priority in respect of land revenue, by resorting to Section 10, he must first take the necessary steps and thereupon only, in respect of the amount of the land revenue, a paramount charge comes into existence. In the present case there has been no default in payment of instalments and consequently there has arisen no occasion to serve a notice of demand, much less a notice of demand as prescribed in Section 10. The argument therefore is quite unsustainable.

The second branch of this argument was that under the Transfer of Property Act, as the vendor was unpaid he had a charge in respect of the balance of the purchase price. This contention can be supported only if there has occurred passing of ownership of the property to the buyer before payment of the whole of the purchase money. A perusal of the agreement in question shows clearly that the ownership of this property cannot pass to the assessee until the lease is granted to him. Under clauses 3 and 5 of the agreement read with Schedule III the right of the assessee to obtain the lease arises only on his completing the property according to the agreement and the approved plans and paying all sums due under the agreement. It was argued on behalf of the assessee that the payments must be of the instalments due till the completion of the structure. In my opinion, that argument is unsound because clause 3 does not limit the payments till the completion of the building. Moreover the terms of the lease only provide for payment of Re. 1 per year, if demanded. The form of lease annexed to the agreement does not provide for payment of the instalments for the years mentioned in the agreement between the parties. It seems that the right to obtain the lease arises only on payment of the full amount of the premium and not on payment of certain instalments only. The agreement read as a whole does not show that there has ever been any intention of passing of ownership of the leasehold to the assessee till the whole premium is paid. It seems therefore clear that as there is no question of passing of ownership till all the instalments are paid the question of creation of a charge under the Transfer of Property Act does not arise. As no charge is thus created, either under the Land Revenue Code or the Transfer of Property Act, the interest paid cannot be considered as paid in respect of the charge subsisting on the property. On the same reasoning the interest

cannot be considered as paid in respect of the property "acquired" under the last sentence of Section 9 (1) (*iv*) of the Act. The property is not acquired till all the instalments and all interest due are paid. I therefore agree that the answer to the question referred to us should be in the negative. The assessee to pay the costs of the reference.

Reference answered in the negative.

[IN THE BOMBAY HIGH COURT.].

LOYAL MOTOR SERVICE CO., LTD.

v.

COMMISSIONER OF INCOME-TAX.

SIR LEONARD STONE, C.J., and KANIA, J. March 5, 1946.

INDIAN INCOME-TAX ACT (XI OF 1922), SECS. 7, 10 (2) (*x*)—DEDUCTIONS —BONUS—SHAREHOLDER EMPLOYEES—BONUS BASED ON SALARY—WHETHER ALLOWABLE DEDUCTION—"SUCH SUM," MEANING OF.

Section 10 (2) (x) of the Indian Income-tax Act must be strictly construed in favour of the subject. The sum excepted under the expression "such sum" in this clause must be the same sum as is described by the expression "any sum paid as bonus or commission." It refers to the quantum and not the character of the payment.

The assessee, a private limited company carrying on the business of passenger transport, was formed by fourteen persons, thirteen of whom were originally owner-drivers of motor vehicles. The thirteen members contributed their vehicles to the company and became its employees while the fourteenth member contributed in money. There were also twenty-eight other employees. In the year in question the assessee paid bonus to its forty-one employees at the rate of two months' salary and the thirteen shareholder employees received Rs. 4,130 as bonus. The quantum of the bonus paid to each of the shareholder employees was by reference to their salaries and not to their stakes in the company. Six of them got less bonus than they would have got as dividends if the sum of Rs. 4,130 had been distributed by way of additional dividends. Five of them got more bonus than such dividends and in the case of two of them the figure worked out the same. The Income-tax authorities contended that the sum of Rs. 4,130 should not be deducted under Section 10 (2) (x) of the Income-tax Act inasmuch as such sum would have been payable to the thirteen shareholders as profits or dividends if the same had not been paid to them as bonus:

Held, *that the whole sum of Rs. 4,130 paid as bonus to the shareholder employees was allowable as deduction under Section 10 (2) (x).*

Reference under Section 66 (1) of the Indian Income-tax Act (XI of 1922) by the Income-tax Appellate Tribunal, Bombay: (Income-tax Reference No. 8 of 1945).

STATEMENT OF CASE.

"Under Section 66 (1) of the Indian Income-tax Act (as amended in 1939), we submit the following case together with a question of law for the opinion of their Lordships of the High Court of Bombay, at the instance of the Loyal Motor Service Co., Ltd., which is the assessee. The question arises out of our judgment in the appeal (R. A. A. No. 148-Bombay 1944-45) brought by the Income-tax Department in connection with the assessee company's assessment for the financial year 1943-44.

2. The following is an agreed statement of facts:—

Several owners of motor vehicles used to individually ply them for passenger transport on certain specified routes in the Poona District. Some time ago, they combined and formed themselves into a private limited company called the Loyal Motor Service Co., Ltd. They made over their vehicles to the company receiving in return the company's shares of equivalent value. Since then the company is carrying on the business of passenger transport. It has engaged a number of employees, about 41, as drivers, mechanics, supervisors, etc., out of whom, in the account year, 13 were the shareholders of the company being the former owners of the motor vehicles. The employees are paid salaries in which there was an all round increase in the year of account. Also, the company paid each of them a bonus equal to 2 months' salary.

In its assessment for 1943-44 the assessee company claimed a deduction of the amounts of salary and bonus in the computation of its business income. The Income-tax Officer allowed the full amount of salary as well as the bonus paid to the employees other than shareholders. In the case of the shareholder employees, however, he allowed only the pre-increased salary and half the increase given in the account year and disallowed the the whole of the bonus amounting to Rs. 4,130. The officer thought that the increase in the salary of the shareholder employees was abnormal and also doubted if they had rendered any exceptional services entitling them to the bonus. On appeal, the Appellate Assistant Commissioner allowed the increase in the salaries to the extent of Rs. 390 and also the whole of the bonus, the latter on the ground that it was fair and reasonable. Copies of their respective orders are exhibits A and B in the annexure.

The Income-tax Officer appealed to the Tribunal from the Appellate Assistant Commissioner's order and the contest was confined to the allowance of the bonus alone. The only point that the Department urged before us was that the bonus was not admissible deduction under Section 10 (2) of the Indian Income-tax Act. In particular, it was pointed out that a

primary condition to the allowance of a bonus paid to an employee is that such sum would not have been payable to him as profits or dividend if it had not been paid as bonus or commission. The employees in question were the shareholders of the company, and it was argued that the amount of Rs. 4,130, coming as it did out of the company's profits would have been distributed as dividend among the shareholder employees, if the company's profits had not been depleted to that extent by the payment of the bonus. We accepted the Department's contention on the point. It was argued on behalf of the assessee that the disallowance should at least be limited to such sum as would be distributable as dividends among the 13 shareholder employees in particular. And, in this connection, stress was laid upon the term 'such' in Section 10 (2) (*x*) of the Indian Income-tax Act. We did not accept this contention and allowed the Department's appeal. Our reasons will be found in paragraph 4 of our judgment, a copy of which is exhibit C.

3. Being dissatisfied with our decision the assessee company made an application, exhibit D, asking us to state a case to the High Court. It is a long and argumentative document. A question is formulated in paragraph 6 which, however, is expressed in a somewhat abstract form. We prefer the form of question proposed by the Commissioner of Income-tax, in his written answer, exhibit E, with a slight modification. We accordingly submit the following question for their Lordships' opinion.

Question referred.—'Whether in the circumstances of the case the sum of Rs. 4,130 paid as bonus to the shareholder employees of the assessee company in the account year is allowable as deduction under the provisions of Section 10 (2) (*x*) of the Indian Income-tax Act, 1922?'"

Sir Jamshedji Kanga, for the assessee.

M. C. Setalvad, for the Commissioner.

JUDGMENT.

STONE, C. J.—This is a reference made to us under Section 66 (1) of the Indian Income-tax Act, by the Income-tax Appellate Tribunal at Bombay. The assessment out of which the question arises is the assessment upon the Loyal Motor Service Co., Ltd., in respect of the financial year 1943-44 of that company, and the question formulated is in these terms:—

"Whether in the circumstances of the case the sum of Rs. 4,130 paid as bonus to the shareholder employees of the assessee company in the account year is allowable as deduction under the provisions of Section 10 (2) (*x*) of the Indian Income-tax Act, 1922?"

The question raised is a short one but it is not one which is free from difficulty. The Indian Income-tax Act provides by Section 6 for five heads of income, profits or gains to be brought to tax and the first head is

"Salaries" whilst the fourth is "Profits and gains of business, profession or vocation."

It is Section 7 which deals with salaries and it is to be noted that "salary" includes a gratuity and a commission. Section 10 provides that tax shall be payable by an assessee under the head profits and gains of business, profession or vocation in respect of the profits and gains of any business carried on by him, and by sub-section (2) of that section it is provided that such profits and gains shall be computed after making the allowances set out in a number of sub-paragraphs, the one with which we are concerned being paragraph (*x*), which says :—

"any sum paid to an employee as bonus or commission for services rendered, where such sum would not have been payable to him as profits or dividend if it had not been paid as bonus or commission."

Now the facts as shown by the reference are that this company was formed by fourteen persons, thirteen of whom were originally owner-drivers of motor vehicles, the fourteenth member contributing in money. The thirteen not only contributed their motor vehicles but also their services and accordingly became employees of this company. Besides the thirteen there are twenty-eight other employees making a total of forty-one. In the year in question the company granted a bonus at the rate of two months' salary to its forty-one employees and the total sum required to pay this bonus was Rs. 6,084, of which Rs. 1,954 went to the twenty-eight other employees and Rs. 4,130 to the thirteen shareholder employees. It is to be noted that the quantum of bonus paid to each of the shareholder employees was by reference to their salaries and not to their stakes in the company. A tabulated result is set out in the application for this reference and is printed on page 12 of the record. It is there shown that of the thirteen shareholder employees six employees got less bonus than they would have got as dividends if the sum of Rs. 4,130 had been distributed by way of additional dividends. Five of them got more bonus than such dividends and in the case of two of them the figure works out the same. That is an accident in the sense that the bonus payment being referential to their wages and the dividends being referential to their shares have no relation to each other. Now the answer to the question referred to us depends on the construction that is to be placed upon para. (*x*) of sub-section (2) of Section 10. It should be noted that the body of this sub-section provides an allowance and the qualifying part of it is by way of exception to that allowance. What is to be allowed is "any sum" paid to an employee as bonus or commission for services rendered and the exception is, where "such sum" would not have been paid to him as profits or dividends if it had not been paid as bonus or commission. In the exception the words "such sum" can, in my opinion, only refer to the last and the only

antecedent, which is " any sum " paid as commission or bonus. Therefore unless the commission or bonus would be paid to the assessee as profits or dividends the exception to the allowance does not operate. Mr. Setalvad on behalf of the Commissioner has pointed out with considerable force that strictly construed there can hardly ever be a case which comes within the ambit of the exception. Sir Jamshedji Kanga on behalf of the assessee company suggests two such cases, *viz.*, in the case of what is generally called a one-man-company which is not unlawful under the Indian Companies Act, and also in a case in which a company, in declaring a dividend, or a partnership, in declaring division of their profits, say that instead of distributing their profits by way of dividends, or shares of profits, they will distribute the amount to themselves, as salaried employees in their own company, or partnership, as bonus. We are construing a taxation statute and the subject is entitled to have such a statute strictly construed in his favour. In my opinion in placing a strict construction on this sub-section, the sum excepted under the expression " such sum " must be the same sum as is described by the expression " any sum paid as bonus or commission," and that an equivalent sum even in the two cases where by accident the bonus and the prospective dividend are the same, is not included in that construction. If that is the construction which is to be placed upon this sub-section, then the answer to the question is, that the whole of the sum of Rs. 4,130 paid as bonus to the shareholder employees is allowable as deduction under the provisions of Section 10 (2) (*x*). I answer the question referred to us in the affirmative. The Commissioner must pay the costs of this reference.

KANIA, J.—In submitting the question for the Court's consideration the Tribunal, in the statement of facts, has stated as follows:—

" Several owners of motor vehicles used to individually ply them for passenger transport on certain specified routes in the Poona District. Some time ago, they combined and formed themselves into a private limited company called the Loyal Motor Service Co., Ltd. They made over their vehicles to the company, receiving in return the company's shares of equivalent value. Since then the company is carrying on the business of passenger transport. It has engaged a number of employees, about forty-one, as drivers, mechanics, supervisers, etc., out of whom, in the account year, thirteen were the shareholders of the company being the former owners of the motor vehicles. The employees are paid salaries in which there was an all round increase in the year of account. Also, the company paid each of them a bonus equal to two months' salary."

It appears that the company claimed deduction in respect of the salaries paid to the employees and after some discussion that question was set at rest. The next question debated was in respect of the bonus paid to the

thirteen shareholder employees. There is no dispute about the others. On behalf of the assessee company it was contended that it was an allowance permitted to be deducted under Section 10 (2) (x) of the Indian Income-tax Act. That clause runs as follows:—

"(x) Any sum paid to an employee as bonus or commission for services rendered, where such sum would not have been payable to him as profits or dividend if it had not been paid as bonus or commission:

Provided that the amount of the bonus or commission is of a reasonable amount with reference to—

(a) the pay of the employee and the conditions of his service;

(b) the profits of the business, profession or vocation for the year in question; and

(c) the general practice in similar businesses, professions or vocations."

On behalf of the assessee company it was pointed out that as the sum was paid as bonus to all employees, it was a permissible allowance under the clause. Having regard to the fact that out of forty-one employees thirteen were shareholders of the company it was contended on behalf of the taxing authority that such sums would have been payable to the thirteen shareholders as profits or dividends, if the same had not been paid to them as bonus. On that ground they contend that while the payment of bonus to non-shareholders was a legitimate deduction, the bonus paid to the shareholders was not permitted to be deducted under the clause. In the process of assessment at one stage this bonus was allowed to be deducted. The Income-tax Officer being dissatisfied with it took the matter to the higher officer. When the matter came before the Tribunal the Department rested their clain on a ground, which, according to the judgment of the Tribunal, was raised for the first time before them. It was argued that "such sum" referred to the character of the payment and not the quantum. It was therefore contended that the amount, if it was capable of reaching the hands of the shareholders, was not permitted to be deducted, if paid as bonus to the shareholders. It was argued that it was outside the scope of Section 10 (2) (x). The argument found favour with the Tribunal.

In my opinion, that construction of the clause is not correct. The word "such" must refer to what had been previously mentioned in the same clause in connection with the word "sum." To find that out we must look to the first part of the clause. That refers to "any" sum. Reading the clause in that way the plain meaning appears to be that when a particular amount was paid by way of bonus to an employee, if the same amount would have been paid to him as a shareholder as dividend or profit, the company cannot be allowed a deduction on the ground of payment of bonus. To put it in other words the clause is intended to prevent an escape from taxation by describing a payment as bonus, when in fact

ordinarily it should have reached the shareholder as profit or dividend. The argument would be equally applicable in the case of a partnership as in the case of a limited company. This construction leads to no hardship. It does not allow a wrong payment of bonus to escape taxation. In the first instance the bonus in the hands of the employee is liable to be taxed, unless exempted by a special notification. Moreover, the proviso contains conditions under which if a wrong claim is made, the same can be investigated and disallowed. An illustration will perhaps make the position clear. Five persons in a firm realising that the profits of the year were Rs. 50,000 and they had an equal share in the profits of the business decide that instead of receiving Rs. 10,000 each as the share of profits each of them will be paid Rs. 10,000 as bonus or commission. In such a case the firm, when sought to be assessed, may contend that Rs. 10,000 were paid as bonus. The contention will be clearly rejected. But the safeguards do not end there. The firm will have to prove to the satisfaction of the taxing authority that the five partners were employees, in the first instance. Secondly, that the bonus was a reasonable amount having regard to the pay of the employee and the conditions of his service. Thirdly, that the profits of the business for the year in question made it reasonable to pay the amount granted as allowance; and lastly, the general practice in similar businesses or trade justified the payment of the amount as bonus. It seems to me that the plain reading of the clause means that the profits of a business will not be allowed to be dwindled by merely describing the payment as bonus, if the payment is in lieu of dividend or profit. I do not see any reason why any strained construction should be put on the plain meaning of the words of the clause. I therefore agree with the learned Chief Justice with regard to the answer to be given to the question referred to us.

Reference answered accordingly.

[IN THE BOMBAY HIGH COURT.]

P. M. HUTHEESINGH & SONS LTD.

v.

COMMISSIONER OF INCOME TAX.

KANIA, Ag. C. J., and CHAGLA, J.

September 20, 1945.

INDIAN INCOME-TAX ACT (XI OF 1922), SECS. 23-A, 66—COMPANY—POWER TO ASSESS INDIVIDUAL MEMBERS—WHETHER PUBLIC ARE SUBSTANTIALLY INTERESTED—BURDEN OF PROOF—WHETHER SHARES WERE DEALT WITH IN STOCK EXCHANGE—QUESTION OF FACT—STATEMENT OF CASE—DUTY OF TRIBUNAL.

The burden of proving that Section 23-A (1) does not apply to a company as it is a company in which the public are substantially interested within the meaning of the explanation to that section is clearly on the company.

The question whether the shares of a company have in the course of the previous years been the subject of dealings in any stock exchange in British India or not is a pure question of fact. As an advisory body the High Court has no jurisdiction to disturb or go behind the findings of fact by the Tribunal. The High Court can only consider whether there was any evidence on which the conclusion can be based.

It is the duty of the Tribunal when they submit a statement of case to the High Court to state the facts clearly, carefully and precisely.

Held, *on the facts of the case, that the assessee company was a company in which the public were not substantially interested within the meaning of the explanation (b) to sub-section (1) of Section 23-A of the Indian Income-tax Act.*

Reference under Section 66 (1) of the Indian Income-tax Act (XI of 1922) by the Income-tax Appellate Tribunal: (Income-tax Reference No. 5 of 1945).

STATEMENT OF CASE.

"The above two reference applications are made by Messrs. P. M. Hutheesingh & Sons Ltd., asking us to refer to the High Court of Bombay certain questions of law which are stated to arise from our judgment in 23-A (1) C. A. Nos. 1 and 2 (Bombay) of 1943-44. As the point arising is common to both the applications it will be convenient to make a consolidated reference.

2. Messrs. P. M. Hutheesingh & Sons Ltd., is a private limited company. They are the managing agents of the Aruna Mills Ltd. The authorised capital of the company is Rs. 1,000 which is divided into 750 promoters' shares of Re. 1 each and 250 ordinary shares of Re. 1 each. All the 750 promoters' shares were taken up by eleven persons at the time of the first allotment made by the company. With the exception of Narotam Lalbhai, none of the holders of the promoters' shares applied for ordinary shares. Narotam Lalbhai was allotted 94 promoters' shares and 1 ordinary share.

3. Section 23-A (1) of the Income-tax Act provides as follows:—

"Where the Income-tax Officer is satisfied that in respect of any previous year the profits and gains distributed as dividends by any company up to the end of the sixth month after its accounts for that previous year are laid before the company in general meeting increased by any income-tax payable thereon are less than sixty per cent. of the assessable income of the company of that previous year, he shall, unless he is satisfied that

having regard to losses incurred by the company in earlier years or to the smallness of the profit made, the payment of a dividend or a larger dividend than that declared would be unreasonable, make with the previous approval of the Inspecting Assistant Commissioner an order in writing that the undistributed portion of the assessable income of the company of that previous year as computed for income-tax purposes shall be deemed to have been distributed as dividends amongst the shareholders as at the date of the general meeting aforesaid, and thereupon the proportionate share thereof of each shareholder shall be included in the total income of such shareholder for the purpose of assessing his total income."

And the last proviso further provides that this sub-section shall not apply to any company in which the public are substantially interested. The explanation (*b*) to the above sub-section defines such a company as follows:—

"A company shall be deemed to be a company in which the public are substantially interested if shares of the company......carrying not less than twenty-five per cent of the voting power have been allotted unconditionally to, or acquired unconditionally by, and are at the end of the previous year beneficially held by, the public......and if any such shares have in the course of such previous year been the subject of dealings in any stock exchange in British India or are in fact freely transferable by the holders to other members of the public."

In the present case, after obtaining the sanction of the Inspecting Assistant Commissioner, the Income-tax Officer held that this company was a company in which the public were not substantially interested, and levied the assessment accordingly.

4. The assessees contended that both the promoters' shares and the ordinary shares were held by the public within the meaning of the explanation (*b*) to sub-section (1) of Section 23-A of the Income-tax Act. In the alternative, it was claimed that even if the 750 promoters' shares were not held by the public the remaining 250 ordinary shares were held by the public. Therefore, it was claimed that this was a company in which the public are substantially interested, and the provisions of the above sub-section are not applicable to their case.

5. We held that the 750 promoters' shares were in fact not freely transferable by the holders to other members of the public and our reasons are contained in para. 8 of our judgment. As regards the 250 ordinary shares we were also of the opinion that, prima facie, they are not freely transferable, and the point has been dealt by us in para. 9 of our judgment. We have also held that it was not proved that the ordinary shares of Messrs. P. M. Hutheesingh & Sons Ltd., have been the subject of dealings in any stock exchange in British India, or were, in fact, not freely transferable

by the holders to the members of the public. We further came to the conclusion that the one ordinary share held by Narotam Lalbhai was not a share held by a member of the public, and our reasons are contained in para. 13 of our judgment. Finally we decided that this is a company in which the public are not substantially interested and the Income-tax Officer was right in applying Section 23-A (1) of the Income-tax Act to the assessment of the applicant company.

6. The following question of law arises from our judgment which we refer to the High Court of Bombay under Section 66 (1) of the Indian Income tax Act :—

Question referred.—' Whether, in the circumstances of the case, it has been rightly held that the assessee company is a company in which the public are not substantially interested within the meaning of the explanation (*b*) to sub-section (1) of Section 23-A of the Indian Income-tax Act ?' "

K. M. Munshi, for the assessees.

M. C. Setalvad, for the Commissioner.

JUDGMENT.

KANIA, AG. C. J.—This is a reference under Section 66 (1) of the Indian Income-tax Act by the Income-tax Appellate Tribunal for the opinion of the Court on the following question :—

" Whether, in the circumstances of the case, it has been rightly held that the assessee company is a company in which the public are not substantially interested within the meaning of the explanation (*b*) to sub-section (1) of Section 23-A of the Indian Income-tax Act ? "

The question relates to the assessment years 1939-40 and 1940-41, and the previous years in question therefore are the calendar years 1938 and 1939. The relevant facts as can be gathered from the statement of case and the judgment are these: Messrs. P. M. Hutheesingh & Sons Ltd., are a limited company. The share capital of Rs. 1,000 is divided into one thousand shares of Re. 1 each, out of which 750 are promoters' shares and 250 are ordinary shares. The 750 promoters' shares were taken up by the eleven persons at the time the first allotment was made by the company. Mr. Narotam Lalbhai was one of the persons to whom 94 promoters' shares were allotted. The 250 ordinary shares of the company were issued in the ordinary course and one share was applied for and allotted to Mr. Narotam Lalbhai. None of the holders of the other promoters' shares applied for any ordinary shares. The company was incorporated in 1928. The memorandum of association of the company shows that before the formation of this company the partnership firm of Messrs. P. M. Hutheesingh & Sons was doing business. It appears that the Aruna Mills Ltd. was then floated and the assessee company were to work as the managing

agents of the Aruna Mills. In the years 1938 and 1939 one ordinary share was held by Mr. Narotam Lalbhai while the remaining 249 shares were held by the members of the public. The taxing authorities considered that the profits of the assessee company were not distributed in the normal way, and acting under Section 23-A (1) an order was passed directing that the proportionate share of the profits which were not distributed should be considered as the income of each shareholder and included in the total income for the purpose of assessing his total income. The relevant provisions of the Income-tax Act are in Section 23-A (1) which runs as follows :—

"Where the Income-tax Officer is satisfied that in respect of any previous year the profits and gains distributed as dividends by any company up to the end of the sixth month after its accounts for that previous year are laid before the company in general meeting increased by any income-tax payable thereon are less than sixty per cent. of the assessable income of the company of that previous year, he shall, unless he is satisfied that having regard to losses incurred by the company in earlier years or to the smallness of the profit made, the payment of a dividend or a larger dividend than that declared would be unreasonable, make with the previous approval of the Inspecting Assistant Commissioner an order in writing that the undistributed portion of the assessable income of the company of that previous year as computed for income-tax purposes shall be deemed to have been distributed as dividends amongst the shareholders as at the date of the general meeting aforesaid, and thereupon the proportionate share thereof of each shareholder shall be included in the total income of such shareholder for the purpose of assessing his total income."

Proviso 3 to that sub-section, which is relevant for the present discussion, is in these terms :—

"Provided further that this sub-section shall not apply to any company in which the public are substantially interested........."

Explanation (*b*) to that proviso runs in these terms :—

"A company shall be deemed to be a company in which the public are substantially interested if shares of the company......carrying not less than twenty-five per cent. of the voting power have been allotted unconditionally to, or acquired unconditionally by, and are at the end of the previous year beneficially held by, the public......and if any such shares have in the course of such previous year been the subject of dealings in any stock exchange in British India or are in fact freely transferable by the holders to other members of the public."

On behalf of the assessees it was contended that Section 23-A (1) did not apply to this company as it was a company in which the public are substantially interested within the meaning of the explanation. The burden of proving this is clearly on the company. In order to establish that

the assessees are such a company, according to the words of the explanation, they have to establish that shares of the company carrying not less than 25 per cent. of the voting power have been allotted (1) unconditionally to, or acquired unconditionally by, *and* (2) are at the end of the previous year beneficially held by—the public; *and* (3) such shares (a) have in the course of such previous year been the subject of dealings in any stock exchange in British India, *or* (b) are in fact freely transferable by the holders to other members of the public.

In order to find out the necessary facts articles 3 and 6 of the articles of association of the company are relevant to be considered. They are in these terms:—

"3. There shall be maintained by or at the instance of each of ordinary shareholder a deposit in the Aruna Mills Ltd., of a sum of Rs. 2,000 for each ordinary share of this company. The said deposit shall be continued and shall not be liable to be paid for a term of 7 years from the date or dates on which the deposit monies shall have been paid. The depositor shall get thereon from the said Aruna Mills Ltd., interest at the rate of 6 per cent. per annum for the deposit, which interest, he will be at liberty to draw at the end of each year.

6. No holder of promoters' shares shall transfer, by way of sale his promoters' shares to any person other than a holder of promoters' shares unless, he first offers the same to such holders at a price not exceeding ten times the average dividend declared or to be declared for the three years immediately preceding the sale and unless the acceptance of such offer is communicated in writing by any one or more of such holders within a fortnight of the receipt of such offer. In the case of a larger number of holders accepting the offer, the transferor will have the right to select, at his absolute discretion and choice, his transferee or transferees. And no shareholder, whether a holder of promoters' shares or otherwise, shall be entitled to transfer the shares standing in his name to any person who is not a member of the company except with the express permission of the directors."

In order to prove that in the course of such previous years the shares were the subject of dealings in any stock exchange in British India, the assessee produced a letter from the president of the Ahmedabad Share and Stock Brokers' Association dated 4th March, 1944. That is addressed to the assessee company and is in the following terms:—

"In reply to your letter.........I am to state that the shares of your company (Aruna Commission Shares) are amongst the securities dealt with on the cash section of my Association. It is a practice with my Association to issue a daily official list of closing prices of shares on the forward list only. Hence no quotation is given in the daily official list of

closing prices of shares of your company. However I am in a position to state that the transactions in the shares of your company (Aruna Commission Shares) were frequently being engaged in by members of my Association *inter se* during the course of the years 1938 and 1939."

The assessee further filed a statement showing the transfers of shares which took place in 1938 and 1939 from the shareholders who were on the list in the previous years and the balance sheets showing transfer fees earned by the company in respect of such transfers of shares.

The assessee company contended that although there might be difficulty in respect of the 750 promoters' shares, the 250 ordinary shares were held by members of the public and that brought them within the words "carrying not less than twenty-five per cent. of the voting power," of the explanation referred to above. It was therefore contended that Section 23-A did not apply to them. On behalf of the Commissioner this position was disputed. It was not admitted that having regard to the articles of association the allotment of shares was unconditional, or that the shares were acquired unconditionally by members of the public at the end of the relevant two years. It was not admitted that such shares were in the course of such years the subject of dealings in any stock exchange in British India, or were in fact freely transferable by the holders to other members of the public. In this connection it was pointed out that under article 3 there was an obligation on the holder of each ordinary share to make a deposit of Rs. 2,000 with the Aruna Mills and which deposit was not liable to be repaid for a term of seven years. It was further pointed out that under article 6 the ordinary shares were not capable of being transferred to a non-member without the express permission of the directors. It was therefore contended that there was no unconditional allotment or unconditional acquisition of shares by the public within the meaning of the explanation. Relying on the same facts it was contended on behalf of the Commissioner that the shares were in fact not freely transferable by the holders to other members of the public. In respect of the evidence led on behalf of the assessee company on the question whether the shares had in the course of previous years been the subject of dealings in any stock exchange in British India, it was contended before the Tribunal that this had not been established by the assessee company.

I must point out here that both in the statement of case and in the judgment there are certain inaccuracies. When a fact finding authority is in the position of the Tribunal (whose findings of fact are considered conclusive), it is always very desirable for them to be accurate in their statement of facts. Under rule 55 framed by the Tribunal for preparing a statement of case to be submitted to Court, there is power to have an agreed statement, if possible, with the assistance of the parties. It is a

desirable and wholesome provision which may be usefully borne in mind so that the contesting parties may have no grievance when the matter is discussed before the High Court. It prevents the contention that a certain material and relevant fact is omitted to be stated, or in fact is not correctly stated having regard to the documents before the Tribunal.

Keeping these inaccuracies apart in the present case the Tribunal has come to two conclusions. At the end of para. 9 of their judgment they have stated that all the 250 shares are not freely transferable. At the end of para. 12 of the judgment they have further stated as follows:—

"In these circumstances we are of opinion that it is not proved that the ordinary shares of Messrs. P. M. Hutheesingh & Sons Ltd., have been the subject of dealings in any stock exchange in British India or in fact freely transferable by the holders to other members of the public."

The first statement about the 250 shares not being freely transferable is a result of the construction of articles 3 and 6 of the articles of association of the company. That is not seriously challenged. The other conclusion is very strongly attacked by the assessee company before us. The question whether such shares have in the course of the previous years been the subject of dealings in any stock exchange in British India or not is a pure question of fact. As an advisory body we have no jurisdiction to disturb or go behind the findings of fact by the Tribunal. We can only consider whether there was any evidence on which the conclusion can be based? In the present case in paragraph 11 of the judgment the Tribunal has stated that the statement filed by the assessee company shows that during the calendar year 1938 eleven transfers in all involving 29 shares took place. We are told that this is a misstatement on the part of the Tribunal. The statement in fact shows transfers of twenty-four shares. The original statement is now produced before us and shows that the assessee is correct. In para. 12 of its judgment the Tribunal has considered the letter of the president of the Ahmedabad Stock Exchange dated 4th March, 1944, mentioned above. The criticism of the Tribunal on the assessee company being called "Aruna Commission" appears to be based on a misreading of the letter. The letter is addressed to the limited company and there are express references to the shares of that company. The words "Aruna Commission Shares," which are put in brackets, only describe the right of the shareholders, according to what is conveniently described as the effect of the memorandum and articles of association of the company. The rest of the criticism of that letter is based on the actual wording of the letter. It shows that the Tribunal fully considered the effect of the letter. It is pointed out that the letter does not show if it refers to the promoters' shares or ordinary shares. It was therefore not considered satisfactory evidence in respect of the ordinary shares, as contended by the assessee

company. It was further pointed out, that the statement in this letter that the transfers of the shares of the assessee company were frequently being engaged in by members of the Association during the years 1938 and 1939 was incorrect, because according to the assessee's own admission the share register showed transfer of three shares only in 1939. That again may be in one lot or in more than one lot. The Tribunal therefore criticized this statement and considered it unreliable or insufficient in any event. Now the burden of proof being on the assessee it was the duty of the assessee to lead evidence to show that in the course of the previous years these ordinary shares had been the subject of dealings in the Ahmedabad Stock Exchange. This letter does not show that the Ahmedabad Stock Exchange maintains a register of actual transactions in the ordinary shares. The president who signed the letter does not say that he himself had effected any transactions in any of these shares in either of the two years. The effect only is that some members of the Association had told the president that there were many transactions. It is on that information that the president wrote this letter. It is clear that if the transactions having in fact been effected on the stock exchange is sought to be proved such information evidence of a person who had not been engaged in any transaction is far from satisfactory or sufficient. We cannot say that the Tribunal in the circumstances was in error in holding that the allegation of the assessee was not proved. We cannot say that there was no evidence before the Tribunal on which they could come to that conclusion. As the assessee had failed to establish the necessary facts which it was their duty to establish before the Tribunal we cannot go behind that conclusion of the Tribunal. The answer to the question referred to us under the circumstances must be in the affirmative. The assessee company must pay the costs of the reference.

CHAGLA, J.—I agree. I would like to join the learned Chief Justice in emphasizing the duty cast upon the Appellate Tribunal with regard to findings of facts. Under the Act it is the final fact finding authority and I think it is the duty of the Tribunal when they submit a statement of case to the High Court to state the facts clearly, carefully and precisely. After all the High Court only exercises an advisory jurisdiction. Its jurisdiction is to advise the Tribunal on questions of law submitted to it and that advisory jurisdiction cannot be exercised usefully unless the fact finding authority submits the facts carefully, clearly and accurately. I am sorry to say that in the reference with which we are dealing both in the statement of case and in the judgment there are several inaccuracies which in some cases are patent. A little more care would have been sufficient to make the Tribunal realise that the statement of facts prepared by them was not as correct and as satisfactory as it should have been. I hope that

in future the Tribunal will bear this in mind when preparing the statement of case.

Reference answered in the affirmative.

[IN THE BOMBAY HIGH COURT.]

BABULAL KANJI *v.* COMMISSIONER OF INCOME-TAX, BOMBAY.

SIR LEONARD STONE, C.J., and KANIA, J. March 5, 1946.

INDIAN INCOME-TAX ACT (XI OF 1922), SEC. 15 (1)—EXEMPTIONS—LIFE INSURANCE PREMIA—POLICY CONTAINING STIPULATION THAT ASSURED SHALL TAKE COMPULSORY LOAN OF 95 PER CENT. OF EACH PREMIUM AT 6¼ PER CENT. INTEREST—95 PER CENT. WHETHER EXEMPT FROM TAX—ESSENTIALS OF LIFE INSURANCE POLICY.

A policy of insurance taken by the assessee in an insurance company recited that it was an assurance on the life of the assessee and it matured on the death of the assured, but there was a condition in the policy that a compulsory loan of 95 per cent. of the premium carrying interest at 6¼ per cent. per annum should be taken by the assured within a week of the payment of each premium on the security of the policy only and that failure to raise such loans would make the policy null and void :

Held, *that the 95 per cent. of the premia which was the subject-matter of the compulsory loans was not paid by the assessee to effect an insurance on his life within the meaning of sub-section (1) of Section 15 of the Indian Income-tax Act and accordingly only the remaining 5 per cent. of the total premia was a permissible deduction under the said sub-section.*

Held also, *that the policy was a life insurance policy notwithstanding the fact that, taking into account the rate of interest on the loan, the assured in any eventuality had to pay more than he could possibly receive.*

Cases referred to :—

Flood *v.* Irish Provident Assurance Co., Ltd. (1912) 46 I.L.T. 214.

Gould *v.* Curtis ([1913] 3 K.B. 84 ; 82 L.J.K.B. 802 ; 180 L.T. 779 ; 6 Tax Cas. 293).

Hunter *v.* Rex ([1902] 2 K.B. 255 ; [1903] 1 K.B. 514 ; [1904] A.C. 161).

Joseph *v.* Law Integrity Insurance Company Limited ([1912] 2 Ch. 581 ; 82 L.J. Ch. 187 ; 107 L.T. 538 ; 20 Mans. 85).

National Standard Life Assurance Corporation, *In re* [1918] 1 Ch. 427.

Paterson *v.* Powell [1832] (9 Bing. 320 ; 2 Moo. & S. 399 ; 2 L.J.C.P. 13 ; 131 E.R. 635).

Provident Insurance Company *v.* Inland Revenue Commissioners ([1904] 2 K.B. 658).

Reference under Section 66 (1) of the Indian Income-tax Act (XI of 1922) by the Income-tax Appellate Tribunal : (Income-tax Reference No. 7 of 1945).

STATEMENT OF CASE.

"This is an application under Section 66 (1), requiring the Tribunal to refer to the High Court of Judicature a question of law arising out of the orders of the Tribunal in R. A. A. No. 27 (Bombay) of 1944-45.

2. In the course of the assessment proceedings for the year 1943-44, the assessee claimed an abatement of Rs. 724 in respect of the insurance premia paid by him. This claim was allowed by the Income-tax Officer, who completed the assessment on 13th August 1943. A further claim in respect of a sum of Rs. 5,813, representing insurance premia paid by the assessee to the Tropical Insurance Company, was made before the Appellate Assistant Commissioner, who allowed the claim and ordered that a sum of Rs. 5,276 was to be further allowed which would make up the statutory limit of Rs. 6,000, when added to the sum of Rs. 724 already allowed by the Income-tax Officer. Against the order of the Appellate Assistant Commissioner, the Income-tax Officer preferred an appeal to the Tribunal.

3. The Tribunal found that the scheme of the Tropical Insurance Company under which a policy of life insurance was effected amounted to no more than an accommodation granted by the company to the assessee for the purpose of enabling him to reduce his income-tax liability. For this accommodation the insurance company charged a fee. The Tribunal further found that even though from the point of view of the company the contract in question might be a life insurance policy, the assured in his turn could not and did not look for any benefits at any stage during the pendency of the policy or at the maturity thereof beyond the expectation of reducing his income-tax liability. The Tribunal examined in detail the scheme under which the insurance company offered the policies known as the 'Businessman's Own Policies' and arrived at the following findings of facts :—

"(1) That the Tropical Insurance Co. has a scheme described as the 'Businessman's Own Policy' scheme. According to this scheme, the minimum amount for which a policy is issued is Rs. 20,000 and the term of the policy is 5 years. The annual premium is Rs. 193-12-0 per thousand and the benefits provided under the policy are as follows :—

(*a*) On death within five years : (per thousand of the sum assured)

Rs. 190 if death occurs in the first year;

Rs. 387 if death occurs in the second year;

Rs. 595 if death occurs in the third year;

Rs. 810 if death occurs in the fourth year;

(*b*) On survivance or death in the fifth year : Full sum assured.

Under the scheme a compulsory loan of 95 per cent. of the premium paid has to be taken by the assured within a week of the payment of each premium on the security of the policy only.

The loan is subjected to an interest of 6 per cent. per annum. No medical examination is necessary under the scheme. The liability of the company in each successive year in relation to the premia received and the

interest debited to the assured on account of the compulsory loan is as below:— .

	Premium and Interest.			Liability.		
	RS.	A.	P.	RS.	A.	P.
1st year ...	6,157	10	0	5,700	0	0
2nd year ...	12,315	4	0	11,610	0	0
3rd year ...	18,472	14	0	17,850	0	0
4th year ...	24,630	8	0	24,300	0	0
5th year ...	30,788	2	0	30,000	0	0

(2) That the company at no stage incurs the risk of having to pay more than the amount actually received from the assured. The only real benefit that the assured counts upon under this scheme is a substantial relief towards his income-tax liability."

The Tribunal further found that although technically speaking the assessee made a full payment of Rs. 5,276, the transaction in substance amounted only to a payment which represented 5 per cent. of that sum, the balance being a complusory loan which the assured was compelled to take. Reading Section 15 (1) of the Income-tax Act in the light of the facts set out above, the Tribunal came to the conclusion that the claim made by the assessee was not covered by Section 15 (1) under which provision only such payments as are made with the object of effecting an insurance on the life of the assessee can be considered. In that view, the Tribunal reversed the Appellate Assistant Commissioner's order.

4. In our opinion, the following question of law arises out of the orders of the Tribunal in R. A. A. No. 27-(Bombay) of 1944-45, which we refer under Section 66 (1) to the High Court of Judicature at Bombay :—

'Whether, upon the facts found by the Tribunal, the sum of Rs. 5,276 is a permissible deduction under Section 15 (1) of the Income-tax Act.'"

Sir Jamshedji Kanga, for the assessee.

M. C. Setalvad, for the Commissioner.

JUDGMENT.

STONE, C. J.—This is a reference under Section 66 of the Indian Income-tax Act and the question referred to us is, whether, upon the facts found by the Tribunal, the sum of Rs. 5,276 is a permissible deduction under Section 15 (1) of the Indian Income-tax Act. The sum of Rs. 5,276 represents the larger sum of Rs. 5,813, being the total annual premium of the policy of insurance to which I am about to refer. The sum of Rs. 5,813 has been scaled down to Rs. 5,276, because the assessee has another insurance policy and the premiums on the two policies added together exceed the total exemption allowed by the Income-tax Act. The question as framed in this reference in substance raises two questions of law for our consideration, first, has there been an insurance on the life of the assessee, and, if so, secondly, what was the amount of the annual premium paid in

the accounting year, which is 1942-43, for effecting such insurance. The relevant section of the Act provides :—

"15. (1) The tax shall not be payable in respect of any sums paid by an assessee to effect an insurance on the life of the assessee or on the life of a wife or husband of the assessee or in respect of a contract for a deferred annuity on the life of the assessee" and so on.

The important words are "paid by an assessee to effect an insurance on the life of the assessee." So that the first question I have formulated demands a consideration whether the policy in this case effects an insurance contingent on the duration of human life. The policy, which is called a "Businessman's own policy without profits," commences by reciting that "Whereas the person named and described in the schedule hereunder (hereinafter called 'the assured') has proposed an assurance on his life with the Tropical Insurance Company Limited." Then under the heading of "Details of sum assured" we find the sub-heading "Date of maturity," and underneath that, "in the event of the death of the assured before maturity" and then is set out in a table the sums which will be paid at the end of the first year, second year, third year and the fourth year, with a proviso in the same portion of the policy "Provided that the above amounts shall be payable only after deducting the loan and interest and current year's premium (if any) then standing against the policy." In another division against the marginal note, "To whom payable" are the words, "To the life assured if alive at the date of maturity or else to his nominee, executors, administrators or legal heirs at earlier death." Against the marginal note, "Events in which payable," is "Survivance of the life assured to the date of maturity or his earlier death." Then under a separate heading "Details of premium," is marginal note, "Special provisions," and, "This policy is issued subject to the conditions that a compulsory loan of ninety-five per cent. of the premium will be taken by the assured within a week of the payment of each premium on the security of the policy as stipulated in privileges and conditions overleaf under the heading 'Loans'." Turning to the back of the policy, there are set out various numbered paragraphs headed, "Privileges and Conditions." Paragraph No. 8, which is called, "Paid-up value," provides : "Since the payment of loan is made compulsory, the policy does not acquire paid-up value" and then comes a very important paragraph, paragraph 9, "Loans":

"A compulsory loan of 95 per cent. of the premium will have to be taken by the assured within a week of the payment of each premium on the security of policy only. Loan will be subject to an interest of 6½ per cent. per annum payable half-yearly on 30th June and 31st December each year.

Failure to raise loan or pay premia or interest will make the policy null and void."

By paragraph 11 the assured agrees that,

"If at any time due to non-payment of interest, the amount of loan with interest accumulation exceeds the surrender value of the policy at the time, the policy shall become liable to forfeiture without notice and in security of the said advance of Rs.......interest and expenses."

A curious feature of this policy is, that taking into account the interest on the compulsory loan at six and a quarter per cent. per annum, the assured, in any eventuality, pays out more than he can possibly receive. At the end of five years, assuming that the assured survives, the policy matures, and the assured will have paid Rs. 968-12-0 in premium for every Rs. 1,000 insured and in addition he will have paid Rs. 57-6-0 by way of interest on the compulsory loans making together the sum of Rs. 1,026-2-0. For this outlay he will receive the sum of Rs. 1,000. Similar results will be found to prevail, if calculations are made at any previous periods up to the maturity of the policy.

We have been referred to the definition in Mr. Bunyon's well-known book on Life Assurance, where at page 1 the learned author says:—

"The contract of life insurance may be further defined to be that in which one party agrees to pay a given sum upon the happening of a particular event contingent upon the duration of human life, in consideration of the immediate payment of a smaller sum or certain equivalent periodical payments by another."

That definition was quoted with approval in the case of *Joseph* v. *Law Integrity Insurance Company, Limited*[1], in which case Cozens-Hardy, M.R., said:—

"I therefore think that these policies are life policies within the meaning of the passage in Bunyon on Life Assurance which I have read. Their effect is to constitute an agreement by the defendant company to pay a given sum on the happening of the particular event contingent on the duration of the life."

It is to be observed that the element upon which Mr. Setalvad for the Commissioner relies, namely that the sum assured must be larger than the sum or sums paid and which finds support in Mr. Bunyon's definition is omitted from that passage, and also that when the facts of *Joseph's* case and also those in the Irish case of *Flood* v. *Irish Provident Assurance Co. Ltd.*[2], quoted in the footnote in *Joseph's* case at page 597, are examined it will be found that the sums paid to effect the insurance in those cases were larger than the sums assured. In *Joseph's* case the payments made under that policy in the first five years amounted to £ 6-10-0, whilst the sum assured at the end of five years was only £ 6: see also *National Standard Life Assurance Corporation, In re*[3].

(1) [1912] 2 Ch. 581, at p. 593.
(2) (1912) 46 I.L.T. 214.
(3) [1918] 1 Ch. 427.

But apart from the authorities, the terms of the policy which we have to consider itself afford a clear indication as to the nature of the policy. The recital, as I have already mentioned, describes it as an assurance on the life of the assured and the policy matures on death. Both these features are the clearest indications that the policy is of life insurance within the meaning of Section 15 of the Act.

That, however, does not dispose of the whole matter since the question remains as to what is the sum or sums paid by the assessee to effect this life insurance. Looking at the substance of the transaction, it is clear that the assessee's income is not diminished by more than five per cent. of the premium which he has to pay each year, the balance, *viz.*, ninety-five per cent. being taken up under the compulsory loan. In my opinion this second question as to the amount paid to effect the policy can be examined in the light of an English decision, *viz.*, the case of *Hunter* v. *Rex*[1]. In that case the Earl of Halsbury, L. C., with characteristic terseness says this:—

"My Lords, it appears to me that this judgment ought to be affirmed. The whole point is that the exemption or deduction, or whatever it is to be called, is to be allowed to the assured if the premium has been 'paid by him'; and the whole reason I give for my judgment is that it has not been paid by him."

Lord Robertson, at page 164, after agreeing with the motion proposed, said :—

"The whole argument of the appellant has been that, in a question between the assured and the insurance company, he must be held to have paid the larger sum. But in point of fact, in a question of the extent by which his income was diminished during the year by the payment, there can be no doubt that it was only by £ 33, and not by £ 66."

In that case there was a loan of half the premium, that is to say, £ 33, though the loan did not have to be taken up compulsorily. That authority must be applied with the caution that we are considering the Indian Income-tax Act and that the whole structure and schemes of the English Income Tax Acts are quite different. But in my opinion the principle we have to consider in this case is the same, since it cannot be said that the ninety-five per cent. of the premia, which are the subject-matter of the compulsory loans and which render the policy null and void if they are not raised as loans, are sums paid by the assessee to effect the insurance. Accordingly, in my opinion the question should be answered by saying that only the five per cent. of the total premium, which is not the subject-matter of the compulsory loan, is a permissible deduction under Section 15 (1) of the Act. A further point has been taken in this Court, *viz.*, that the

(1) [1902] 2 K.B. 255 on appeal [1903] 1 K.B. 514 and on appeal to the House of Lords [1904] A.C. 161, at p. 162.

amount of interest paid each year on the compulsory loan is also a permissible deduction. I think in the peculiar circumstances of this case it may very well be that it is, but the question referred to us does not embrace any such sum and I am unwilling as a general proposition to lay down about it anything that might be taken as a precedent. Assessee to get three-fourths of the costs.

KANIA, J.—The question submitted for the Court's opinion is to be determined in the light of Section 15 (1) of the Indian Income-tax Act. It is there provided that the tax shall not be payable in respect of any sums paid by an assessee to effect an insurance on the life of the assessee. The rest of the section is not material to the present discussion. The relevant provisions of the policy of insurance, in respect of which the question is submitted for our opinion, have been set out in the judgment of the learned Chief Justice. I should like to draw attention to two more facts in this connection. The premium agreed to be paid is uniform for five years and is fixed at Rs. 193-12-0 per thousand. The second point which is made clear by the express terms of the policy is that in the event of the death of the assured before maturity, in the first year, the company agreed to pay Rs. 190 for every one thousand rupees. If a similar contingency happened in the second year it agreed to pay Rs. 387, in the third year Rs. 595 and in the fourth year Rs. 810. These figures show that if death occurred during the first two years, apart from the question of loan, the assured will get less than the premium paid by him. On the other hand, if death occurred during the third or fourth years, his representatives would get more than the premia paid by the assessee.

Having regard to the terms of this policy of insurance, it appears that two questions have to be determined under Section 15 (1) of the Indian Income-tax Act. The first is whether there is an insurance on the life of the assessee. The second is what sum, if any, he has paid in the accounting year to effect such life assurance.

It appears to have been argued before the Tribunal, as it was also argued before us, that this is not a contract of life insurance. In support of that contention it was pointed out that because of the compulsory provision to take a loan and pay interest thereon, in no circumstances the assured received from the insurance company more than what he paid at any time. It was therefore contended that under no circumstances the interest of the company was adversely affected under the scheme and therefore the company took no risk, and there was no contract of insurance. In support of this contention the statement in Bunyon's Life Assurance about a policy of insurance was relied upon. The statement runs as follows :—

"The contract of life insurance may be further defined to be that in which one party agrees to pay a given sum upon the happening of a

particular event contingent upon the duration of human life, in consideration of the immediate payment of a smaller sum or certain equivalent periodical payments by another."

A reference to the statement in Bunyon discloses that the learned author had quoted these words from the judgment of Tindal, C.J., in *Paterson* v. *Powell* [1]. In that case the contract was in these terms :—

" In consideration of forty guineas for £ 100, and according to that rate for every greater or less sum, received of . . . . we have hereunto subscribed our names . . . . and will pay, or cause to be paid unto the said . . . . the sum and sums of money, which we have hereunto respectively subscribed, without any abatement whatever."

The question was whether this was a policy of insurance and if so void under 14 Geo. III, c. 4. In describing the effect of the transaction contained in the document, the learned Chief Justice observed that it was a contract to pay a larger sum in consideration of payment of smaller sums. On going through the judgment it is clear that the learned Chief Justice had not expressed the view that payment of a smaller sum was a necessary ingredient to make it a contract of insurance. The question as to what would be required to constitute a contract of insurance came to be fully considered in *Prudential Insurance Company* v. *Inland Revenue Commissioners*[2]. In a carefully considered judgment which, except on one point, has been accepted by the highest judicial authority, Channell, J., observed as follows :—

" The Attorney-General says that to constitute a contract of insurance it must be a provision against something—against some loss or disadvantageous event. Mr. Danckwerts says that may be true as regards marine and fire policies which are indemnities against loss, but it is not true as regards life policies, for a policy of life insurance is not a contract of indemnity. But the question is whether that makes any real difference, and it seems to me that we must inquire a little further into the nature of a contract of insurance. Where you insure a ship or a house you cannot insure that the ship shall not be lost or the house burnt, but what you do insure is that a sum of money shall be paid upon the happening of a certain event. That I think is the first requirement in a contract of insurance. It must be a contract whereby for some consideration, usually but not necessarily for periodical payments called premiums, you secure to yourself some benefit, usually but not necessarily the payment of a sum of money, upon the happening of some event. Then the next thing that is necessary is that the event should be one which involves some amount of uncertainty. There must be either uncertainty whether the event will ever happen or

(1) (1832) 9 Bing. 320, at p. 321. (2) [1904] 2 K.B. 658, at p. 662.

not, or if the event is one which must happen at some time there must be uncertainty as to the time at which it will happen."

This definition given by Mr. Justice Channell is accepted by the House of Lords. The learned Judge then continued as follows (p. 663):—

"The remaining essential is that which was referred to by the Attorney-General when he said the insurance must be against something. A contract which would otherwise be a mere wager may become an insurance by reason of the assured having an interest in the subject-matter—that is to say, the uncertain event which is necessary to make the contract amount to an insurance must be an event which is *prima facie* adverse to the interest of the assured. The insurance is to provide for the payment of a sum of money to meet a loss or detriment which will or may be suffered upon the happening of the event."

In the case before the learned Judge he was of the view that in respect of a person agreeing to pay 6d. a week, he must be poor and, therefore, the provision in the policy to pay him a certain sum in the event of his attaining a certain age was a contract against his interest. He stated as follows (p. 664):—

"The reaching of that age, with its attendant disadvantages, is to my mind an event which is sufficiently adverse to the interest of a poor person to make it a proper subject against which to insure."

This observation was considered in *Gould* v. *Curtis*[1]. Cozens-Hardy, M. R., who was a party to *Joseph* v. *Law Integrity Insurance Company, Limited*[2], in which the definition of a policy of life assurance given by Mr. Justice Channell was approved, was faced with the question of the element of the adverse interest of the assessee to constitute a policy of life assurance. In the course of argument Lord Justice Buckley pointed out that in *Prudential Insurance Co.* v. *Inland Revenue Commissioners*[3], Mr. Justice Channell had stated that a contract of insurance must be a contract for the payment of a sum of money, or for some corresponding benefit to become due on the happening of an event, which event must be of a character more or less adverse to the interest of the person effecting the insurance. The reply given by counsel was that this was dissented from in the Irish case reported in the note to *Joseph* v. *Law Integrity Insurance Company, Limited*[2]. In the course of his judgment Cozens-Hardy, M. R., while approving of the passage previously cited in *Joseph's* case, dealt with the question of adverse interest in the following terms (p. 92):—

"It has been suggested that this cannot be a contract of insurance because the continuance of life is not an event which can be fairly said to be adverse to the interests of the insurer. This is based really upon a passage in the judgment of Channell, J., in the *Prudential Company's* case.

(1) [1913] 3 K.B. 84. (2) [1912] 2 Ch. 581. (3) [1904] 2 K.B. 658.

He was there dealing with an argument which had been addressed to him by counsel. Dealing with the case of an insurance by a man who was of the artisan class, with small weekly payments, he pointed out that a payment made to a man in that class when he attains sixty-five, or whatever the age might be, is one which may be fairly said to contemplate an adverse event to the man who probably might not then be able so well to maintain himself and his wife. If, however, the learned Judge intended to lay down that there cannot be a contract of insurance unless the event is of a character more or less adverse to the interests of the person effecting the assurance, with the greatest possible respect to the learned Judge, I do not think that is accurate. I do not think it is true to say that there can be no insurance except the event covered by the contract is one which is in its nature adverse to the assured."

The result of these authorities, therefore, is that, while the contract must be that, in consideration of a sum of money paid in one sum or by different instalments, the company agrees to pay another sum on the happening of a contingent event, and which event must be connected with the life of the assured, the factor of the contract being necessarily disadvantageous to the assessee, is not a necessary ingredient. In the present case, therefore, the contention, that because in no event the assessee can receive more from the insurance company than what he pays, there is no policy of insurance is unsound. In my opinion, that argument is not relevant to decide the question whether the contract is one of life insurance or not. In the present case the other essential ingredients, according to the judgment of Mr. Justice Channell, are found in the policy. I am therefore clearly of the opinion that the policy of assurance is a life insurance policy.

That leaves for consideration the second question according to the words of Section 15 (1) of the Indian Income-tax Act. The question is, in the accounting year, what sums were paid by the assessee to effect the insurance. We are concerned only with the year in question and the terms of the policy contained in the document before us. It was argued on behalf of the assessee that he paid the premium to effect an insurance on his life and therefore under Section 15 (1) of the Indian Income-tax Act that whole amount was exempt from taxation. It was argued that the provision relating to loan was an independent transaction which had nothing to do with effecting the insurance. The fact of the insurance company giving a full receipt for the payment of the premium and the fact of the compulsory loan being taken within a week were strongly relied upon in this connection. While those two factors have to be taken into consideration, it seems equally clear that the contract of insurance contains reciprocal terms and the term to pay the premium is not the only condition made by the assured for obtaining the policy on his life. The different clauses

must be read as forming part of one promise to pay the sum on which the assured obtains a policy on his life. I do not think there can be any doubt on that question. If authority is needed, the same is found in *Hunter* v. *Rex*[1]. In that case the agreement between the assured and the company was that the premium was to be paid by half the amount being paid in cash and the company giving credit to the assured for the other half and on which the assured agreed to pay four per cent. interest. It must be noticed that the contract in that case provided for this loan being a voluntary transaction. The assured was not obliged to take the loan at all. If, however, he took the loan, the payment of premium was to be worked out as stated above. On those facts the Court came to the conclusion that the assured paid half the premium. He did not pay the other half to obtain the policy of insurance. It may be noticed that Lord Davey in delivering judgment also took into consideration the question of the loan being recalled. Lord Davey observed (p. 163) :—

"It may be that the insured was liable to be sued for that £ 33 [being half the premium of the year]; but he was willing to run that risk, no doubt, for the sake of obtaining the very favourable terms which were offered to him by the insurance company, who were not likely to injure their business by taking such a step."

In the present case, therefore, we have to consider what sum the assured had agreed to pay to effect insurance on his life in the year in question. As a life insurance policy may cover a period of five or ten years and the premium may be payable every year, it seems to me that the word "effect" in Section 15 (1) must include also maintaining an insurance on the life of the assessee. The question, therefore, is what sum was paid by the assessee in the accounting year to maintain the insurance on his life. We are concerned with the policy before us and the payments made under the same. The premium paid at the rate of Rs. 193-12-0 per one thousand rupees is clearly to be considered as a payment made to effect the insurance. But the contract does not end there. The contract provides that the insurance company must give a loan to the assured of 95 per cent. of the premium. Although clause 9 of the privileges and conditions does not in terms say that the company has to give the loan, it provides that failure to raise the loan or pay premium or interest will make the policy null and void. Raising the loan requires the consent of two parties, the person asking for the loan and the person giving the loan. As this is made a condition of the subsistence of the policy, it seems clear that the company initially agreed to give the loan also. Clause 8 of the same privileges and conditions further supports this construction. It says : " Since the payment of loan

(1) [1904] A.C. 161.

is made compulsory, the policy does not acquire paid-up value." It therefore not only envisages the grant of a loan but the subsistence of the loan throughout the period. Even if it is argued that there being no express words showing that the loan must continue throughout the period and therefore the company had a right to call back the loan, the contract contained in this policy is in any event for the payment of a premium followed by a refund of ninety-five per cent. thereof by the company to the assured within a week. Thus the net balance of five per cent. of the premia only is left in the hands of the company.

In respect of the loan the further provision is that failure to pay interest will make the policy void. The interest can be payable only if a loan is subsisting and to the extent it is subsisting. Under the express terms of clause 9 it seems to me therefore that in respect of this policy payment of interest, as the payment of premium, are both made conditions for the subsistence of the policy, and therefore if in addition to the five per cent. premium, which remains in the hands of the company, the assured has to pay and in fact has paid interest on the loan to the company, it will be a payment made by the assured to effect or maintain the insurance on his life. In that view calculations will have to be made and exemption granted. We are not concerned with the actual amounts for which exemption has to be granted. It is sufficient to express the opinion that on the wording of this policy the answer to the question, what sum is paid by the assured to maintain the life insurance policy in the year in question, is the premium, less the loan, plus the interest paid by him during the accounting year. The limit of Rs. 6,000 is fixed by the Act and the necessary adjustments will have to be made on that basis.

Reference answered accordingly.

[IN THE PATNA HIGH COURT.]

RAJA BAHADUR KAMAKSHYA NARAIN SINGH

v.

COMMISSIONER OF INCOME-TAX, BIHAR AND ORISSA.

MANOHAR LALL, AG. C.J., and DAS, J.

August 22, 1946.

INDIAN INCOME-TAX ACT (XI OF 1922), SECS. 2 (1), 4 (3) (*viii*), 22 (1) AND (2)—NET RECEIPTS FROM SALE OF FOREST TREES—WHETHER INCOME OR CAPITAL—INTEREST ON ARREARS OF RENT AND CESS—WHETHER AGRICULTURAL INCOME—NOTICE UNDER SECTION 22 (2) AND SUBMISSION OF RETURN—CONTENTION THAT NOTICE UNDER SECTION 22 (1) IS INVALID—LEGALITY.

The net receipts from the sale of forest trees are income liable to income-tax and are not capital receipts.

Interest on arrears of rent and cess relating to agricultural land is agricultural income within the meaning of Section 2 (1) of the Indian Income-tax Act and, as such, exempt from tax under Section 4 (3) (viii).

Where the assessee has been served with a notice under Section 22 (2) and he has filed a return it is not open to him to object to the assessment merely on the ground that the notice under Section 22 (1) was issued irregularly.

Cases referred to:—

Commissioner of Income-tax *v.* Manavedan Tirumalpad [1930] (A.I.R. 1930 Mad. 764; 126 I.C. 596; 4 I.T.C. 421; I.L.R. 54 Mad. 21).

Kesho Prashad Singh *v.* Sheo Pragash Ojha [1921] (I.L.R. 44 All. 19 approved by P.C. in I.L.R. 46 All. 831; A.I.R. 1924 P.C. 247; 51 I.A. 381; 82 I.C. 962).

Province of Bihar *v.* Maharaja Pratap Udai Nath Sahi Deo of Ratugarh [1941] (9 I.T.R. 313; 20 Pat. 699; 194 I.C. 203; 4 F.L.J. (H.C.) 109; 22 P.L.T. 485; A.I.R. 1941 Pat. 289).

Srimath Jagathguru Sringeri Sri Satchitanantha Chandrasekara Bharati Swamigal *v.* C. P. Duraiswami Naidu [1931] (A.I.R. 1931 Mad. 659; 54 Mad. 900; 134 I.C. 42).

Srimati Lakshmi Daiji *v.* Commissioner of Income-tax, Bihar and Orissa [1944] (12 I.T.R. 309).

Reference under Section 66 (1) of the Indian Income-tax Act (XI of 1922) by the Income-tax Appellate Tribunal, Bombay: (Miscellaneous Judicial Case No. 87 of 1945).

STATEMENT OF CASE.

"These two applications under Section 66 (1) relate to the assessment made for the charge year 1942-43. One of them 66 R. A. No. 28-Bihar of 1944-45 is at the instance of the Commissioner of Income-tax, Bihar and Orissa, and the other 66 R. A. No. 40-Bihar of 1944-45 is at the instance of the assessee.

2. For the assessment year 1942-43 assessment was made originally on a total income of Rs. 7,84,565 by the Income-tax Officer, Special Circle, Patna. On appeal to the Appellate Assistant Commissioner the amount was reduced to Rs. 7,79,075 which comprised, *inter alia*, net income from sale of forest trees (Rs. 80,415) and interest on arrears of rent and cess relating to agricultural lands (Rs. 23,539 minus 6 per cent. allowed as collection charges).

3. Thereupon the assessee preferred a second appeal to the Tribunal and the contentions raised by the assessee, so far as material to the present reference, were:—

(*a*) that the receipts from the sale of forest trees were capital and not revenue receipts;

(*b*) that in assessing the net income from forest, expenses incurred in preceding years should have been allowed as deferred revenue expenditure;

(*c*) that interest on arrears of rent and cess relating to agricultural lands was agricultural income within the meaning of Section 2 (1) of the Act and, as such, exempt from tax under Section 4 (3) (*viii*).

(*d*) that the statutory notice under Section 22 (1) of the Act (as amended in 1939) was not properly and validly issued; that, therefore, the notice issued under Section 22 (2) was also not legal and proper;

(*e*) that the Income-tax Officer, Special Circle, Patna, had no jurisdiction to make the assessment and that the whole assessment was liable to be set aside as *ultra vires* and without jurisdiction.

4. The first contention of the assessee was repelled by this Bench of the Tribunal (as it then was constituted) which held that the receipt from forest was 'income' and not the realisation of capital asset. The second objection relating to the disallowance of expenses incurred in past years as deferred revenue expenditure was also overruled on the grounds (i) that expense so incurred can be treated only as the expense of the year in which it was incurred and set off only against the income of such year, and (ii) that the appellant had not shown what the amount of such expense was. The third objection was allowed and the Bench excluded the amount of interest on arrears of rent and cess holding it to be agricultural income within the meaning of Section 2 (1) of the Act. The fourth objection was negatived on the finding that the combined notice issued under Section 22 (1) was a sufficient compliance with the terms of the section. In view of the conclusion reached by the Bench, the other argument that the notice under Section 22 (2) was also invalid was not considered, but the Bench felt 'inclined to think that there is no force in this contention as the Act contemplates consequences of defaults of either notice separately.' The last contention also was not considered inasmuch as the Bench had recorded a definite finding as regards the validity of the notice under Section 22 (1). In the result the appeal was allowed in part.

5. The assessee now makes an application under Section 66 (1) and claims that the following questions of law arise out of that part of the appellate order of the Tribunal which is adverse to him :—

(1) Whether trees of virgin forests and of spontaneous growth are capital assets in the case of original proprietors of the lands on which they stand?

(2) Whether capital is lost or diminished in any way by sale of such trees?

(3) Whether in the circumstances of the case the receipts by sale of such trees are capital or revenue receipts?

(4) Whether the expenditure incurred for protection of such trees are allowable in later years as deferred revenue expenditure as in the case of expenses incurred for cultivation and growth thereof?

(5) Whether in the circumstances of the case the assessment of the applicant by the Income-tax Officer, Special Circle, was competent and with jurisdiction?

6. The Commissioner of Income-tax, Bihar and Orissa, the respondent to this application, in his reply under rule 54 of the Appellate Tribunal Rules, submits that question (iii), which involves questions (i) and (ii), has been set at rest by the decision in the case of *Commissioner of Income-tax* v. *Manavedan*[1], which has been approved of by the Patna High Court in the case of *Province of Bihar* v. *Maharaja Pratap Udai Nath Sahi Deo*[2], that question (iv) is academic in view of the finding by the Bench that the assessee failed to furnish particulars and prove the expenditure, and question (v) is too vague and general and it does not arise out of the appellate order of the Bench, for no question of jurisdiction has been raised and decided by the Bench.

7. Similarly the Commissioner of Income-tax has applied under Section 66 (1) asking us to refer the following question of law to the Hon'ble High Court :—

'Whether interest on arrears of rent is agricultural income within the meaning of Section 2 of the Income-tax Act ?'

8. The assessee, who is respondent to this application, in his reply under rule 54 of the Appellate Tribunal Rules, contends that the Hon'ble High Court has already answered this question in the affirmative in the appellant's case for the charge year 1939-40 ; and, as such, it has ceased to be a referable question of law.

9. As both the applications arise out of the same order of the Tribunal and concern the same assessment, we propose to draw up one statement of the case which would govern both the cases.

10. *66 R. A. No. 40-Bihar of 1944-45.*—We take up the assessee's application first. Questions (i), (ii) and (iii) involve the contention that receipt from forests is in the nature of capital receipt. It is conceded that, if at all it is held to be revenue receipt, it is non-agricultural income liable to tax. It appears that the estate has not only been spending substantial amounts on the maintenance and improvement of the forest, but has been deriving regular income therefrom. In the past, however, such income was not brought under assessment on the mistaken impression that it was exempt from income-tax. The Bench came to the following conclusion :—

(*a*) The land on which forest trees grow stand intact and as this is merely a growth on the land of a spontaneous nature saleable from time to time, it cannot be said to be a capital receipt.

(*b*) In jungles trees grow from time to time and their sale or cutting down does not deprive the owner of any capital asset but the growth may be likened to what is merely the fruits of the trees which are sold; the sources of growth namely, the lands, remain the property of the landlord, and capital is not in any way lost or diminished by the sale of forest trees.

(1) (1930) 4 I.T.C. 421. (2) [1941] 9 I.T.R. 313.

11. The departmental representative argues that the point raised by the applicant is covered by the decision in the case of *Province of Bihar* v. *Maharaja Pratap Udai Nath Sahi Deo*[1]. The finding in this case that receipt from virgin forest is not agricultural income and is, therefore, liable to income-tax, undoubtedly involves the decision that it is not a capital receipt. It must, however, be conceded that the point did not specifically arise for consideration and the decision proceeded on the common ground that such receipt was income. We think that, in the circumstances of this case, the question is one of law and arises out of the order of the Tribunal. We, therefore, refer the following question to the Hon'ble High Court :—

'Whether the assessee's net receipts from the sale of forest trees are the assessee's income liable to income-tax or merely capital receipts ?'

12. Question (iv) raises the point whether expenses incurred on the protection or improvement of the forests in preceding years can be allowed in the assessment year under review as 'deferred revenue expenditure.' The amount of such expenses, according to the assessee, comes to Rs. 3,25,028. The establishment charges incurred during the relevant year of account as also a certain percentage of the gross receipts 'as incidental general management costs' were allowed. But the assessee's claim in regard to 'deferred revenue expenditure' was disallowed. The Income-tax Officer, in disallowing the claim, observed :—

"As to the alternative claim, what exactly the nature of such expenses in the past was and in what way they can be treated as a revenue expenditure, which will have any bearing on earning of this year's income, are not proved, as the accounts are said to be filed in Court. But from the explanations offered by the assessee's representatives, however, it appears that heavy development costs were incurred in the past, which, by no means could be classed as revenue expenditure. The assessee follows cash basis of accounting and only such deductions as are necessary for earning the income could be allowed. Capital expenses in past have to be excluded, and only revenue expenses to be deducted from gross receipts each year to see if there was profit or loss in the year's working (*sic*) in past years leaving anything of what is called 'deferred revenue expenditure for these years' as contended by the assessee. Assessee's accounts show nothing of the kind and the admixture of revenue and capital expenditure in all these years has resulted in a state of affairs, within which it is impossible to verify the truth of assessee's assertions."

The Appellate Assistant Commissioner upheld the disallowance and remarked :—

"Beyond stating these were unabsorbed expenses of the past the assessee is unable to furnish the particulars as the books are said to be in

(1) [1941] 9 I.T.R. 313.

Court. Admittedly, however, there were heavy development costs incurred in the past. Besides, the principle of mercantile accounting for assessing business does not apply to assessment of income from other source. Under Section 12 (2) against income from other source is allowable any expenditure not being of capital nature 'incurred solely for the purpose of making or earning such income'." In second appeal the Bench of the Tribunal held :—

"Expenses so incurred can be treated only as the expense of the year in which it was incurred and set off only against the income of such year. No part of that expense could be claimed as any deferred revenue expenditure for there was no benefit that accrued by the expenditure which continued to be available at any later period. The expense was only for protection of the property and that benefit would cease immediately the staff was withdrawn. Apart from this the appellant has not shown what the amount of such expense claimed is. The entire amount of excess of expenditure over income cannot be considered as expenditure to be considered in connection with the assessment under appeal for if there is any benefit it does not cease with the assessment made."

It follows from these findings that the assessee in point of fact failed to substantiate his claim that the total amount of expenditure, or an ascertainable portion thereof, was revenue expenditure which could be set off against the income of the relevant accounting year. Furthermore, the point, in so far as it raises a broad question of law, is concluded by the decision of their Lordships of the Judicial Committee in the case reported as *Commissioner of Income-tax, U. P.* v. *Basant Rai*[1] and, as such, ceases to be a referable question of law. In these circumstances, we refuse to refer this question to the Hon'ble High Court.

13. The last question, as framed by the assessee, does not arise out of the order under Section 33. Before we deal with the implications inherent in this question we would like to set out the facts on which the assessee's contention appears to have been founded. By a notification dated the 14th September, 1940, the Commissioner of Income-tax created a Special Circle at Patna, and under Section 5 (5) of the Act he directed that the Income-tax Officer in charge of that Circle should perform the functions of an Income-tax Officer (i) in respect of such income and such classes of persons in the area comprised in the Province of Bihar and Orissa as were assessable to excess profits tax under the Excess Profits Tax Act, 1940, and (ii) in respect of all persons and all classes of income liable to income-tax as well, whose income-tax assessment cases will be transferred to his charge by the Commissioner of Income-tax to the exclusion of any other Income-tax Officer or Income-tax Officers appointed in the said area.

(1) [1933] 6 I.T.C. 459 ; 1 I.T.R. 197.

By a further notification dated the 11th of November, 1940, made under Section 5 (5) of the Act, the Commissioner of Income-tax transferred certain specified cases, including the applicant's case, to the Income-tax Officer in charge of the newly created Special Circle and directed that in respect of the applicant's case (*inter alia*) the Income-tax Officer, Hazaribagh, should not exercise the powers of an Income-tax Officer. On the 22nd April, 1942, a combined notice on behalf of several Income-tax Officers under the signature of the then Commissioner of Income-tax was issued in pursuance of the provision of Section 22 (1) of the Act, as amended in 1939. The notice was in the following terms :—

"In pursuance of sub-section (1) of Section 22 of the Indian Income-tax Act, 1922 (XI of 1922), each of the Income-tax Officers mentioned in column 1 of the annexed table hereby gives notice to every person, subject to his jurisdiction as specified in the corresponding entry in column 2 thereof, whose total income during the previous year exceeded the maximum amount not chargeable to income-tax, to furnish to him within 60 days from the date of this notice a return in the prescribed form and verified in the prescribed manner setting forth (along with such other particulars as are required by the said form) the total income and total world income of such person during that year..........."

The Income-tax Officer, Special Circle, Patna, is mentioned in column 1, and his jurisdictional area in column 2. On these facts the assessee maintained that the statutory notice under Section 22 (1) was not validly and properly issued. Our attention has been drawn to rule 18A of the Income-tax Rules which, according to the assessee, contemplates that the notice should be issued under the signature of the Income-tax Officer concerned. It was the assessee's contention, therefore, that the notification issued under the signature of the Commissioner of Income-tax was not a sufficient compliance with the requirements of law. The assessee further urged that, in consequence of the notice under Section 22 (1) being invalid, the notice issued under Section 22 (2) also was illegal and without jurisdiction. The suggestion was that the issue of a notice under sub-section (2) was dependent for its validity on a legal and proper notice under sub-section (1). The contention had for its object the obtaining of a declaration that the proceedings conducted after the issue of the notice under Section 22 (2) were null and void and, therefore, the assessment was liable to be annulled. The question appears to have been raised in the grounds of appeal before the Appellate Assistant Commissioner but there is no discussion of this point in his order. It may be that the plea was later abandoned. Be that as it may, the question was reagitated before the Tribunal and the Bench dealt with the contention which formed the first premise, namely, whether the notice under Section 22 (1) was validly issued. It came to the following conclusion :—

"It appears that the various Income-tax Officers have combined to issue a common notice and have specified the area within the jurisdiction of each one of the officers. The combined notice is merely for the sake of economy. The Income-tax Officer, the area under his jurisdiction and the fact that the notice is by the respective Income-tax Officers against whom his jurisdiction is mentioned are all published and in substance the notice is by the Income-tax Officer under Section 22 (1) as is mentioned in the notice itself. The other argument, therefore, that the notice under Section 22 (2) is invalid if there is no valid notice under Section 22 (1) need not be considered but we are inclined to think that there is no force in this contention as the Act contemplates consequences of defaults of either notice separately."

In view of the decision at which the Tribunal arrived, the further and more important question of whether the assessment proceedings were null and void did not arise for decision. It is doubtful whether the assessee, even if he had succeeded in showing that the notices issued under sub-sections (1) and (2) of Section 22 were not valid, he would have still been able to obtain the relief by getting the assessment annulled. He had responded to the notice under Section 22 (2), which was served on him, by filing a duly verified return and the proceedings continued from that stage in accordance with law. Be that as it may, as we have already pointed out, the only finding recorded by the Bench concerns the validity of the notice under Section 22 (1), and a question of law does arise out of this finding. If, as a result of this reference, it is found that the notice under Section 22 (1) was invalid and inoperative the other questions may have to be examined at a later stage. At the present moment, however, we can only refer to the Hon'ble High Court the following question which can be said to arise out of the Tribunal's order under Section 33 :—

'Whether the statutory notice under Section 22 (1) [of the Act as amended in 1939] was validly and properly issued in respect of the appellant's assessment for 1942-43 ?'

14. *66 R. A. No. 28-Bihar of 1944-45.*—We now take up the Commissioner's application. The only question framed by him raises the point whether 'interest on arrears of rent' relating to agricultural lands is agricultural income and, as such, exempt from tax under Section 4 (3) (*viii*) of the Act. The amount involved is Rs. 23,539 less 6 per cent. allowed as collection charges. This sum, of course, is inclusive of interest on cess and the Commissioner means to refer, in his application, to the aggregate amount. We have already set out the decision of the Tribunal which was to the effect that such interest is agricultural income within the meaning of Section 2 (1) of the Act. The point is concluded by the decision of the Patna High Court in the case reported as *Srimathi Lakshmi*

Daiji v. *Commissioner of Income-tax, Bihar and Orissa*[1], and we would not ordinarily have referred the question once again for the opinion of the Hon'ble High Court, but as we are referring certain other questions at the instance of the assessee and as the question raised by the department arises out of the same order and as the whole case will thus be before the High Court, we desire to refer the question formulated by the Commissioner of Income-tax as well. It may here be mentioned that the Commissioner's point of view is to keep the assessment alive by making it the subject of a pending reference so that if in the meantime the Judicial Committee of the Privy Council were to decide the question in favour of the department the amount of interest now exempted might then be brought under assessment without any legal hitch. We, therefore, formulate the following question of law :—

'Whether interest on arrears of rent and cess relating to agricultural lands is agricultural income within the meaning of Section 2 (1) of the Act and, as such, exempt from tax under Section 4 (3) (*viii*).'

15. Under Section 66 (1) of the Act we, therefore, refer the following questions to the High Court of Judicature at Patna :—

'(1) Whether the assessee's net receipts from the sale of forest trees are the assessee's income liable to income-tax or merely capital receipts ?'

'(2) Whether the statutory notice under Section 22 (1) [of the Act as amended in 1939] was validly and properly issued in respect of the appellant's assessment for 1942-43 ?'

'(3) Whether interest on arrears of rent and cess relating to agricultural lands is agricultural income within the meaning of Section 2 (1) of the Act and, as such, exempt from tax under Section 4 (3) (*viii*) ?' "

L. K. Jha, for the assessee.

S. N. Dutta, for the Commissioner.

JUDGMENT.

MANOHAR LALL, AG. C. J. and DAS, J.—The Appellate Tribunal has referred the following two questions at the instance of the assessee :—

"(1) Whether the assessee's net receipts from the sale of forest trees are the assessee's income liable to income-tax or merely capital receipts ?

(2) Whether the statutory notice under Section 22 (1) [of the Act as amended in 1939] was validly and properly issued in respect of the appellant's assessment for 1942-43 ?"

The third question for our decision referred at the instance of the Commissioner is as follows :—

"Whether interest on arrears of rent and cess relating to agricultural lands is agricultural income within the meaning of Section 2 (1) of the Act and, as such, exempt from tax under Section 4 (3) (*viii*) ?"

(1) [1944] 12 I.T.R. 309.

For the assessment year 1942-43 the assessee, Raja Bahadur Kamakshaya Narain Singh of Ramgarh, was assessed on a total sum of Rs. 7,84,565 which includes a sum of Rs. 84,993 on account of price realised by the sale of forest trees in his zemindary. The claim of the assessee that the sale of forest trees should be treated as a sale of capital asset has been rejected by the Income-tax authorities.

The question was examined by a Special Bench of this Court in the case of *Maharaja Pratap Udai Nath Sahi Deo* [1]. We referred with approval to the Madras case of *Manavedan Tirumalpad* [2] and another Madras case of *Srimath Jagathguru Sringeri* [3] and the Full Bench case of the Allahabad High Court in *Kesho Prashad Singh*[4]; the latter case was approved by their Lordships of the Judicial Committee in I.L.R. 46 Allahabad 831.

Mr. L. K. Jha appearing for the assessee contended that the sale of the forest trees must necessarily result in the diminution of the value of the estate of the assessee and, therefore, the amount realised should be treated as a capital receipt. This argument has been unsuccessfully advanced on a number of occasions as pointed out above and is similar to the argument advanced on behalf of this very assessee that royalties from coal mine should not be assessed to income-tax as the amount received resulted in diminution of the value of the mine by extracting so much coal therefrom.

In our opinion the Income-tax authorities have taken the correct view.

With regard to the invalidity of the notice issued under Section 22 (1) of the Income-tax Act, the facts are these. On the 22nd of April, 1942, the Commissioner of Income-tax issued a notice in pursuance of Section 22 (1) of the Income-tax Act. It was contended that this was not a notice contemplated under Section 22 (1) as the notice was not signed by the Income-tax Officer of the place having jurisdiction in a particular area. But it was not contended that the contents of the notice were not in the proper form or that the notice did not substantially comply with the provisions of Section 22 (1). The Appellate Tribunal did not accept the argument of the assessee in these words: "It appears that the notice purports to be on behalf of the Income-tax Officer though it is signed in the end by the Commissioner of Income-tax. It appears that the various Income-tax Officers have combined to issue a common notice and have specified the area within the jurisdiction of each one of the officers. The combined notice is merely for the sake of economy. The Income-tax Officer, the area under his jurisdiction and the fact that the notice is by the respective Income-tax Officers against whom his jurisdiction is mentioned are all published and in

(1) [1941] 9 I.T.R. 313.
(2) (1930) I.L.R. 54 Mad. 21.
(3) (1931) I.L.R. 54 Mad. 900.
(4) (1921) I.L.R. 44 All. 19.

substance the notice is by the Income-tax Officer under Section 22 (1) as is mentioned in the notice itself."

As in this particular case, the assessee was admittedly served with a notice under Section 22 (2) of the Act and he filed a return, it follows, in our opinion, that it does not lie in the mouth of this assessee to object to the assessment merely on the ground that the notice under Section 22 (1) was issued irregularly, assuming that this was so. In our opinion, the question does not arise for decision, and we decline to answer the question.

It was agreed by the standing counsel that the answer to the third question must be as given by the Special Bench of this Court in the case of *Srimati Lakshmi Daiji* [1], where we held that interest on arrears of rent was agricultural income within the meaning of Section 2 (1) (*a*) of the Indian Income-tax Act. No fresh argument has been advanced before us to induce us to take a view different from that expressed by that Special Bench. For the same reasoning interest on arrears of cess relating to agricultural lands must be held to be agricultural income within the meaning of Section 2 (1) of the Income-tax Act.

The answers to the questions are, therefore, as follows :—

Question No. 1.—The assessee's net receipts from the sale of forest trees are liable to income-tax and are, therefore, not capital receipts.

Question No. 2.—We decline to answer this question.

Question No. 3.—Interest on arrears of rent and cess relating to agricultural lands is agricultural income within the meaning of Section 2 (1) of the Indian Income-tax Act and, as such, exempt from tax under Section 4 (3) (*viii*).

In view of the divided success of both parties, we direct that each party will bear his own costs in this Court.

Reference answered accordingly.

[IN THE PATNA HIGH COURT.]

RAJA BAHADUR KAMAKSHYA NARAIN SINGH

v.

COMMISSIONER OF INCOME TAX, BIHAR & ORISSA.

MANOHAR LALL, AG. C. J., SINHA and DAS, JJ. August 27, 1946.

INDIAN INCOME-TAX ACT (XI OF 1922), SEC. 1—GOVERNMENT OF INDIA ACT, 1935, SEC. 92—EXCLUDED AREA—ASSESSMENT BEFORE APPLYING FINANCE ACT—SUBSEQUENT REGULATION OF GOVERNOR PROVIDING THAT ACT MUST BE DEEMED TO HAVE COME INTO FORCE BEFORE DATE OF ASSESSMENT—VALIDITY OF REGULATION AND ASSESSMENT—CHANGE OF LAW—APPLICABILITY OF NEW LAW TO PENDING PROCEEDINGS—SCOPE OF SEC. 92—RELATION BETWEEN FINANCE ACT AND INCOME-TAX ACT—' DEEMED

(1) [1944] 12 I.T.R. 309.

TO BE,' MEANING OF—CHOTA NAGPUR DIVISION AND THE SANTAL PARGANAS DISTRICT VALIDATING REGULATION (I OF 1941)—CHOTA NAGPUR DIVISION AND THE SANTAL PARGANAS DISTRICT VALIDATING (AMENDMENT) REGULATION (IV OF 1942)—INDIAN FINANCE ACT, 1939.

The assessee who was residing in a partially excluded area in the Province of Bihar was assessed for the year 1939-40 on his income for the year ended 31st March, 1939, on the 14th February, 1940. On the 13th June, 1941, the Governor of Bihar, acting under Section 92 (2) of the Government of India Act, 1935, enacted Regulation I of 1941 which declared inter alia *that the Indian Income-tax (Amendment) Act, 1939, should be deemed to have come into force in the area on the 1st April, 1939. By an oversight the Indian Finance Act of 1939 was not mentioned in this Regulation. On the 30th June, 1942, Regulation IV of 1942 was therefore enacted by the Governor of Bihar with the sanction of the Governor-General and the Regulation provided* inter alia *that the Indian Finance Act, 1939, should be deemed to have come into force in this area on the 30th March, 1939. The assessee contended on appeal that the assessment was* ultra vires *inasmuch as the Indian Finance Act, 1939, was not in operation at the date of the assessment and that the validating Regulations passed by the Bihar Governor were* ultra vires. *The appeal to the Appellate Tribunal was disposed of only on the 31st March, 1943 :*

Held, (*i*) *that the Regulations were* intra vires *the Governor ;*

(*ii*) *that though as a rule no liability to tax attaches until the Finance Act has been enacted, and Regulation IV was passed only in 1942, the assessment made on the 14th February, 1940, was valid in view of the express provision in Regulation IV of 1942 that the Finance Act of 1939 should be deemed to have come into force in the area on the 30th March, 1939. As the assessee had appealed to the Appellate Tribunal and the appeal was pending when Regulation IV of 1942 was enacted the Tribunal was bound to apply the provisions of the Finance Act, 1939, on the date it was asked to declare that the assessment was* ultra vires.

Under Section 92 (2) of the Government of India Act, 1935, the Governor has plenary powers to make any regulation for the peace and good government of an excluded area in his Province with the consent of the Governor-General. Such a Regulation can act retrospectively or retroactively or can come into operation in future or can apply to pending assessments ; and if the very tenor and subject of the Regulation make it obvious that it is for the peace and good government of the area, it is wholly unnecessary to make such a statement in the preamble.

Cases referred to :—

Bhagat Singh *v.* King Emperor [1931] (58 I.A. 169 ; 12 Lah. 280 ; A.I.R. 1931 P.C. 111 ; 131 I.C. 415).

Commissioner of Income-tax, Bombay *v.* The Bombay Trust Corporation Ltd. as agent of the Hong Kong Trust Corporation Ltd. [1930] (4 I.T.C. 312 ; 57 I.A. 49 ; I.L.R. 54 Bom. 216 ; 121 I.C. 532).

Commissioner of Income-tax *v.* Western India Turf Club Ltd. [1928] (52 Bom. 123; 55 I.A. 14; 106 I.C. 642; 30 Bom. L.R 105; A.I.R. 1928 P.C. 1; 2 I.T.C. 490).
Maharajah of Pithapuram *v.* Commissioner of Income-tax, Madras [1945] (13 I.T. R. 221).
Mukerjee, Official Receiver *v.* Ramratan Kuer [1936] (A.I.R. 1936 P.C. 49; 63 I.A. 47).

Reference under Section 66 (1) of the Indian Income-tax Act (XI of 1922) by the Income-tax Appellate Tribunal: (Miscellaneous Judicial Case No. 130 of 1944).

STATEMENT OF CASE.

"Raja Bahadur Kamakshya Narain Singh of Ramgarh Raj by his application dated 3rd July, 1943, filed under Section 66 (1) of the Indian Income-tax Act, 1922, has asked us to state a case to the Honourable High Court of Judicature at Patna on the following questions of law as arising out of our order passed under Section 33 (4) of the Act on 31st March, 1943, in R. A. A. No. 14-Bihar of 1942-43:—

(1) Whether the Governor has plenary legislative powers to make any Act operate retrospectively in partially excluded areas?

(2) Whether any Act can be applied to any partially excluded area without a preliminary notification as contemplated in Section 92 (1) of the Government of India Act?

(3) Whether the Bihar Validating Regulation I of 1941 is within the scope of authority of the Governor of Bihar under Section 92 (2) of the Government of India Act?

(4) Whether the Bihar Validating Regulation No. IV of 1942 is within the competence of the legislative powers of the Governor under Section 92 (2) of the Government of India Act?

2. The Commissioner of Income-tax, Bihar and Orissa, the respondent to this case is of opinion that all these questions are questions of law but as question No. 4 is the same as question No. 3 it need not be referred.

3. The three questions 1 to 3 raised by the applicant can be combined into one: "Is the assessment made valid and legal?" We agree that a question of law does arise in this case. We proceed to state the case as follows:—

4. The applicant is the proprietor of the Ramgarh Raj in the district of Hazaribagh in the Chota Nagpur Division of the Province of Bihar. He was assessed for the year 1939-40 in respect of his income for the year ended 31st March, 1939. Under the Government of India Act, 1935, this place is a "partially excluded area" and to this area only such Acts of the Central Legislature apply as are extended by the Governor of the Province by virtue of power vested in him by Section 92 (1) of the Government of India Act. This section runs as follows:—

"The executive authority of a Province extends to excluded and partially excluded areas therein, but, notwithstanding anything in this Act, no Act

of the Federal Legislature or of the Provincial Legislature shall apply to an excluded area or a partially excluded area, unless the Governor by public notification so directs, and the Governor in giving such a direction with respect to any Act may direct that the Act shall in its application to the area, or to any specified part thereof, have effect subject to such exceptions or modifications as he thinks fit."

The Governor of Bihar on 17th June, 1941, notified the following Regulation called Bihar Regulation I of 1941 :—

BIHAR REGULATION I OF 1941.

THE CHOTA NAGPUR DIVISION AND THE SANTAL PARGANAS DISTRICT VALIDATING REGULATION, 1941.

(Received the assent of the Governor-General on the 13th June, 1941, and was first published in the "Bihar Gazette" Extraordinary, of the 17th June, 1941).

A Regulation to remove doubts as to the operation of certain Acts of the Central Legislature in the partially excluded areas of the Province of Bihar.

Whereas it is expedient to remove doubts as to the operation of certain Acts of the Central Legislature in the partially excluded areas of the Province of Bihar;

It is hereby enacted as follows :—

1. (1) This Regulation may be called the Chota Nagpur Division and the Santal Parganas District Validating Regulation, 1941.

(2) It extends to the Chota Nagpur Division and the Santal Parganas District.

(3) It shall come into force at once.

2. (1) Section 1 and Part 1 of the Indian Income-tax (Amendment) Act, 1939, shall be deemed to have come into force in the area to which the Regulation extends on the 1st day of April 1939 :

Provided that sub-clauses (iii) and (iv) of clause (b) of Section 11 shall not be deemed to have taken effect earlier than the 1st day of April 1940.

(2) Part II of the Indian Income-tax (Amendment) Act, 1939, shall be deemed to have come into force in the said area on the date appointed by the Central Government for its coming into force throughout British India generally.

3. The Income-tax Law Amendment Act, 1940, the Excess Profits Tax Act, 1940, and the Indian Finance Act, 1940, shall be deemed to have come into force in the area to which this Regulation extends on the 26th day of March 1940, the 13th day of April 1940 and the 6th day of April 1940, respectively.

By a Notification No. 133-Leg. R., dated 7th July 1942, the Governor of Bihar promulgated another Regulation called Bihar

Regulation IV of 1942 modifying to some extent the Regulation of 1941 as follows :—

No. 133-Leg. R.—The following Regulation made by the Governor under sub-section (2) of Section 92 of the Government of India Act, 1935, has been assented to by the Governor-General on the 30th June 1942 and is hereby published for general information :—

BIHAR REGULATION IV OF 1942.

THE CHOTA NAGPUR DIVISION AND THE SANTAL PARGANAS DISTRICT VALIDATING (AMENDMENT) REGULATION, 1942.

A Regulation to amend the Chota Nagpur Division and the Santal Parganas District Validating Regulation, 1941, for a certain purpose.

Whereas it is expedient to amend the Chota Nagpur Division and the Santal Parganas District Validating Regulation, 1941, for a certain purpose;

It is hereby enacted as follows :—

1. (1) This Regulation may be called the Chota Nagpur Division and the Santal Parganas District Validating (Amendment) Regulation, 1942.

(2) It shall come into force at once.

2. For Section 3 of the Chota Nagpur Division and Santal Parganas District Validating Regulation, 1941, the following section shall be substituted and shall be deemed always to have been so substituted, namely :—

3. The Indian Finance Act, 1938, the Indian Finance Act, 1939, the Income-tax Law Amendment Act, 1940, the Excess Profits Tax Act, 1940, the Indian Finance Act, 1940, the Indian Finance (No. 2) Act, 1940, and the Indian Finance Act, 1941, shall be deemed to have come into force in the area to which this Regulation extends on the 26th day of March 1938, the 30th day of March 1939, the 26th day of March 1940, the 13th day of April 1940, the 6th day of April 1940, the 29th day of November 1940 and the 31st day of March 1941, respectively.

5. In an appeal under Section 33 before us the applicant raised the following objections :—

(1) For that the learned Income-tax Officer had no jurisdiction to make any assessment for income-tax or super-tax.

(2) For that there is no Notification or Regulation extending the Finance Act of 1939 to the District of Hazaribagh which is part of the Chota Nagpur Division, a partially excluded area, under the Government of India Act, 1935, as required by Section 92 (1). As such no assessment or levy of tax was competent.

(3) For that the provisions of the Income-tax Amending Act of 1939 were also not applicable as no retrospective operation could be given to any Act by a public notification under Section 92 (1) of the Government of India Act.

(4) For that the Validating Ordinance of 1942 is without jurisdiction and could not have the effect of giving retrospective operation to the said Finance Act, 1939.

In our order dated 31st March, 1943, passed under Section 33 (4), we turned down these objections and upheld the assessment. Hence this application.

6. It is the Finance Act which makes the Income-tax Act operative. The assessment concerned in this case is for the assessment year 1939-40 and the Income-tax Officer accordingly applied the rates fixed by the Finance Act of 1939. By the Chota Nagpur Division and the Santal Pargana District Validating (Amendment) Regulation, 1942, quoted in paragraph above, the Finance Act, 1939, was extended to this partially excluded area thus applying the Finance Act, 1939, retrospectively to that area.

7. The argument that the Governor could not apply the Act retrospectively involved considerations of plenary powers of the Governor. We were inclined to think that on the strength of the English case *Queen* v. *Burah* the plenary powers should be considered to be applicable to the excluded and partially excluded areas and we therefore held that the Finance Act 1939, could be taken to be applicable retrospectively. Powers of legislation are practically conferred on the Governor, *i.e.*, he could adopt any Act with such modifications as he liked. He could apply any Act prospectively and also retrospectively.

8. As we think that question of law does arise out of our order under Section 33 (4) in this case, we refer the following question decisive of the issues raised under Section 66 (1) of the Indian Income-tax Act by the applicant to the Honourable High Court of Judicature at Patna :—

'Is the assessment made legal and valid in view of the Bihar Regulations I of 1941 and IV of 1942?'"

Dr. D. N. Mitter, Rai Bahadur P. K. Banerji, L. K. Jha, S. K. Majumdar and *S. P. Singh*, for the assessee.

Baldev Sahay, P. P. Varma and *S. C. Misra*, for the Commissioner.

JUDGMENT.

MANOHAR LALL, AG. C. J.—The Appellate Tribunal has referred to us the following question for our opinion under Section 66 (1) of the Indian Income-tax Act :—

"Is the assessment made legal and valid in view of the Bihar Validating Regulations I of 1941 and IV of 1942?"

It is impossible to get from the papers printed in the paper-book the relevant dates which are necessary to decide the question raised. It is to be regretted that notwithstanding the clear and repeated directions from this Court the Income-tax department persist in sending up an incomplete

(1) (1878) 3 App. Cas. 889.

paper-book. This Court may have to take serious notice in future if the paper-book continues to omit the important orders and documents by mulcting the department in heavy costs to compensate the assessee for the harassment caused by adjourning the hearing of the case.

However, in the present case, the learned Advocates are agreed as to the important dates which are relevant for the purpose.

The assessment year of the assessee is 1939-40 for the accounting year 1938-39, which commenced on the 1st of April, 1938, and ended on the 31st March, 1939. The assessment was completed on the 14th February, 1940. The appeal against the assessment was disposed of on the 7th March, 1942. Two days before, on the 5th of March, 1942, the assessee took an additional ground that the assessment was *ultra vires* inasmuch as the Indian Finance Act of 1939 was not in operation on the date of the assessment, and that the Validating Acts or the Validating Regulations passed by the Bihar Governor were *ultra vires*. The Appellate Assistant Commissioner, whose order is not to be found in the paper-book, dismissed the appeal. The Appellate Tribunal disposed of the appeal of the assessee on the 31st of March, 1943. They came to the conclusion that the Validating Ordinance of 1942, applying the Finance Act of 1939 as well as the Income-tax (Amendment) Act, 1939, with retrospective effect, was *intra vires* of the Governor and made the assessment valid.

It is now convenient to refer to the relevant Acts passed by the Bihar Governor.

On the 13th of June, 1941, the Governor-General gave assent to Bihar Regulation I of 1941. The preamble of the Regulation shows that it was passed to remove doubts as to the operation of certain Acts of the Central Legislature in the partially excluded areas of the Province of Bihar to which the present assessment relates. By Section 2 of the Regulation certain provisions of the Indian Income-tax (Amendment) Act, 1939, were declared to have come into force on the 1st of April, 1939, and by Section 3 the Indian Income-tax Law Amendment Act, 1940, the Excess Profits Tax Act, 1940, and the Indian Finance Act, 1940, shall be deemed to have come into force in these excluded areas on the 26th of March, 1940, the 13th of April, 1940, and the 6th of April, 1940, respectively. By lamentable oversight the Indian Finance Act of 1939 was not mentioned in Section 3 of this Regulation. The result was that Bihar Regulation IV of 1942 had to be enacted by the Governor with the sanction of the Governor-General on the 30th June, 1942. By Section 3 of this Regulation it was provided that the Indian Finance Act, 1938, the Indian Finance Act, 1939, the Income-tax Law Amendment Act, 1940, the Excess Profits Tax Act, 1940, the Indian Finance Act, 1940, the Indian Finance (No. 2) Act, 1940, and the Indian Finance Act, 1941, shall be deemed to have come into force in the excluded areas on the 26th March, 1938, the 30th March,

1939, the 26th March, 1940, the 13th April, 1940, the 6th April, 1940, the 29th November, 1940, and the 31st March, 1941, respectively.

By Section 92 (1) of the Government of India Act, 1935, it is enacted that no Act of the Federal Legislature, or of the Provincial Legislature, shall apply to an excluded area or a partially excluded area, unless the Governor by public notification so directs, and the Governor in giving such a direction with respect to any Act may direct that the Act shall, in its application to the area, or to any specified part thereof, have effect subject to such exceptions or modifications as he thinks fit.

By sub-section (2) of the same section it is provided that the Governor may make Regulations for the peace and good government of any area in a Province which is for the time being an excluded area, or a partially excluded area, and any Regulations so made may repeal or amend any Act of the Federal Legislature or of the Provincial Legislature, or any existing Indian law, which is for the time being applicable to the area in question. It is then provided that Regulations made under this sub-section shall be submitted forthwith to the Governor-General and until he assents shall have no effect.

On these facts the question of law stated above arises for our decision.

Dr. Mitter on behalf of the assessee contends that the assessment is *ultra vires* for the following reasons :—

(i) That the Bihar Governor cannot encroach on the Central field with regard to any item in List I of the Seventh Schedule to the Government of India Act and in particular regarding item 54 "Taxes on income other than agricultural income;" (ii) that if the Regulation is treated to have been passed under Section 92 (1) it is *ultra vires* as the Governor has no power to make the Regulation operate retrospectively; (iii) if however the Regulation is treated to have been passed under Section 92 (2) the assessment is bad as the Governor even with the consent of the Governor-General cannot pass any Regulation which will affect the assessment which had already been completed on the date when this Act came into force; and (iv) the Income-tax Officer could not have applied the Indian Finance Act of 1939 because it was admittedly not in operation when the assessment proceedings began and were completed, and in the alternative the Income-tax Officer could not be deemed to have applied the Indian Finance Act of 1939 because he was not even aware of the existence of that Act on the relevant dates.

Mr. Baldev Sahay, who appeared for the Income-tax department, on the other hand, replied in an able argument that the contentions of the assessee were not sound because the Governor has plenary powers under Section 92 (2) of the Government of India Act to pass any Regulation he likes provided it was for the peace and good government of the particular

areas concerned and it was assented to by the Governor-General. He argues that it cannot be denied that the impugned Regulation was for the peace and good government of the areas covered by the present assessment. He also submitted that the Governor in the excluded area is not controlled by the fetters of any lists in the schedules of the Government of India Act.

In our opinion the argument of Mr. Baldev Sahay is well founded and must prevail.

The impugned Regulation is not passed under Section 92 (1) of the Government of India Act, and, therefore, it is unnecessary to consider the argument of Dr. Mitter that this sub-section cannot authorise the Governor to extend an Act of the Central Legislature so as to operate retrospectively.

But the Governor has unlimited or, as it is called, plenary powers under Section 92 (2) to make any Regulation for the peace and good government of the particular area in his Province. The only fetter is that the Act cannot come into force unless he has obtained the consent of the Governor-General which has been done in this case. As the Governor has plenary powers he can pass any Regulation whether it acts retrospectively or retroactively or is to come into operation in future or is to apply to pending assessments. But it was argued by Dr. Mitter that there was nothing in the preamble of the Act to indicate that it was for the peace and good government of the Province. In our opinion it is wholly unnecessary to make such a statement in the preamble if the very tenor and subject of the Regulation make it obvious that it is for the peace and good government of the area. This view has been taken by the highest authorities in a large number of cases. See, for instance, the case of *Bhagat Singh*[1]. The argument advanced on behalf of the accused in that case was that the Ordinance promulgated by the Governor-General under Section 72 of the Government of India Act, 1915, which authorised him in case of emergency to promulgate Ordinances for the peace and good government of British India was invalid inasmuch as on the facts it could be found that the state of emergency did not exist and that the Ordinance did not conduce to the peace and good government in British India. Viscount Dunedin in delivering the judgment of the Board negatived these two contentions thus at page 171 :—

" The petitioners ask this Board to find that a state of emergency did not exist. That raises directly the question who is to be the judge of whether a state of emergency exists. A state of emergency is something that does not permit of any exact definition. It connotes a state of matters calling for drastic action, which is to be judged as such by some one. It is more than obvious that that some one must be the Governor-General, and he alone. Any other view would render utterly inept the whole provision.

(1) (1931) 58 I.A. 169.

Emergency demands immediate action, and that action is prescribed to be taken by the Governor-General.

It is he alone who can promulgate the Ordinance.

* * * *

In fact, the contention is so completely without foundation on the face of it that it would be idle to allow an appeal to argue about it.

It was next said that the Ordinance did not conduce to the peace and good government of British India. The same remark applies.

The Governor-General is also the judge of that. The power given by Section 72 is an absolute power, without any limits prescribed, except only that it cannot do what the Indian Legislature would be unable to do, although it is made clear that it is only to be used in extreme cases of necessity where the good government of India demands it."

And at page 173 their Lordships added that " although the Governor-General thought fit to expound the reasons which induced him to promulgate this Ordinance, this was not in their Lordships' opinion in any way incumbent on him as a matter of law."

We are also unable to uphold the contention of Dr. Mitter that the Income-tax Officer should not have applied or rather could not apply the provisions of the Indian Finance Act of 1939 before they were extended to this area because the Regulation of 1942 clearly provides that the Indian Finance Act of 1939 shall be deemed to have come into force in the area on the 30th March, 1939. What is the meaning of the words " deemed to be " when found in a statute? The matter was considered by their Lordships of the Judicial Committee in the case of *Commissioner of Income-tax, Bombay* v. *The Bombay Trust Corporation Ltd. as agent of the Hong Kong Trust Corporation Ltd.*[1] The section there under consideration contained the words " for all the purposes of this Act, be deemed to be such agent." Viscount Dunedin made these observations at page 314 : " They are therefore to be ' deemed to be ' the agent who is chargeable to income-tax, are deemed to be the assessee, the assessee being in terms of Section 2 (2) defined as the person by whom income-tax is payable. Now when a person is ' deemed to be ' something, the only meaning possible is that whereas he is not in reality that something the Act of Parliament requires him to be treated as if he were. It follows that although the High Court was perfectly right in holding that if Section 42 stood alone ' agent ' in that section would mean an agent in actual receipt of the profits or gains which were to be assessed, they failed to appreciate that Section 43 puts the person who comes within its terms artificially into the position of the agent and of assessee under Section 42." This is exactly the position here. It is, therefore, not pertinent to point out that on the date when the Income-tax Officer started the assessment the Indian Finance

(1) (1930) 4 I.T.C. 312

Act of 1939 was in reality not in operation because the Regulation of 1942 directs that the Indian Finance Act of 1939 must be deemed to have been in operation on that date. It is also to be observed that the Income-tax Officer actually applied the provisions of the Indian Finance Act of 1939 to the assessment of this assessee believing that the Indian Finance Act of 1939 had been extended to this area so that the assessment of the assessee had been made by him as if the Indian Finance Act of 1939 was actually in operation.

The contention of Dr. Mitter that there is no liability to tax unless the Finance Act has been passed is perfectly correct. In the case of *Western India Turf Club*[1] the Lord Chancellor in delivering the judgment of the Privy Council observed at page 495: "The argument which has been used in favour of the appeal seems to involve the fallacy that liability to tax attached to the income in the previous year. This is not so. No liability to tax attached to the income of this company until the passing of the Act of 1925, and it was then to be taxed at the rate appropriate to a company." The same view was taken by their Lordships of the Judicial Committee in *Maharajah of Pithapuram* v. *Commissioner of Income-tax, Madras*[2]. Lord Thankerton in delivering the judgment of the Board made these observations at page 223: "It should be remembered that the Indian Income-tax Act of 1922, as amended from time to time, forms a code which has no operative effect except so far as it is rendered applicable for the recovery of tax imposed for a particular fiscal year by a Finance Act. This may be illustrated by pointing out that there was no charge on the 1938-39 income either of the appellant or his daughters, nor assessment of such income until the passing of the Indian Finance Act of 1939, which imposed the tax for 1939-40 on the 1938-39 income and authorised the present assessment etc." But this conclusion does not help the assessee because, as already stated, the effect of the Regulation of 1942 is that the Indian Finance Act of 1939 must be deemed to have been in operation on the date when the assessment proceedings started and on the date when they were completed.

The matter may be looked at from yet another point of view. The assessment proceedings had not become final because the assessee had appealed to the Appellate Tribunal and the appeal was actually pending when the Regulation of 1942 was enacted. As the Regulation expressly declared that the Finance Act of 1939 must be deemed to have been in operation from the 30th March, 1939, the Tribunal was in duty bound to apply the provisions of that Act on the date it was asked to declare that the whole assessment was *ultra vires*. This position may be thus illustrated by the case of *Mukerjee, Official Receiver* v. *Ramratan Kuer*.[3] In that case

(1) (1928) 2 I.T.C. 490. (2) [1945] 13 I.T.R. 221. (3) (1936) 63 I A. 47.

during the pendency of the appeal to the Privy Council, the Bihar Tenancy (Amendment) Act, 1934, was passed which inserted Section 26 (N) to the Act which provided that every person claiming an interest as landlord in any holding shall be deemed to have given his consent to every transfer of such holding made before January 1, 1923 etc. The decree of the Subordinate Judge was passed in 1930 several years before the enactment came into force. Sir George Rankin delivering the judgment of the Board observed at page 51: "In these circumstances, it appears to their Lordships that unless some saving can be implied as regards occupancy-holdings which, at the date of the commencement of the Act, are in question in a pending suit, Section 26 (N) must be applied to the present case, and the plaintiff's appeal must fail *in limine*. Their Lordships are of opinion that no such saving can be implied. Section 26 (N) is not a provision to the effect that action shall lie in certain circumstances, nor has it any reference directly to litigation. Its provision is that every person claiming an interest as a landlord shall be deemed to have given his consent to every transfer made before January 1, 1923. This is retrospective: the question is not whether general language shall be taken only in a prospective sense. The object of this section can only be to quiet titles which are more than ten years old, and to ensure that if during those ten years the transferee has not been ejected he shall have the right to remain on the land. Within this class the Legislature has not thought fit to discriminate against tenants whose right is under challenge in a suit, a course which it may well have regarded as invidious or unnecessary. As substantive rights of landlords and their accrued causes of action were to be abrogated, respect for pending suits over old transfers cannot be assumed." It is interesting to observe that Lord Thankerton during the course of the argument observed as follows at page 49: "If the new Act declares that this transaction, being dated in 1916, shall be valid despite the fact that consent is not given by the landlord, would not this Court be bound by that? The duty of a Court is to administer the law of the land at the date when the Court is administering it." Reference was made to *Quiller* v. *Mapleson*[1].

For these reasons the answer to the question is as follows:

The assessment is made legal and valid in view of the Bihar Regulation IV of 1942.

In view of the peculiar circumstances, I would direct that each party shall bear his own costs in this Court.

SINHA, J.—I agree.

DAS, J.—I agree.

Reference answered accordingly.

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(1) (1882) 9 Q. B. D. 672

[IN THE PATNA HIGH COURT.]

CHATTURAM AND OTHERS

v.

COMMISSIONER OF INCOME-TAX, BIHAR AND ORISSA.

MANOHAR LALL, Ag. C. J., SINHA and DAS, JJ. August 27, 1946.

INDIAN INCOME-TAX ACT (XI OF 1922), SECS. 1, 22 (1) & (2)—GOVERNMENT OF INDIA ACT, 1935, SEC. 92—CHOTA NAGPUR AND SANTAL PARGANAS DISTRICT VALIDATING REGULATION (I OF 1941)—EXCLUDED AREA—SUBMISSION OF RETURN IN PURSUANCE OF NOTICE ISSUED BEFORE EXTENDING FINANCE ACT TO THAT AREA—NOTIFICATION AND REGULATION APPLYING FINANCE ACT RETROSPECTIVELY—VALIDITY OF ASSESSMENT AND NOTICES UNDER SECTIONS 22 (1) AND (2).

On the 20th April, 1940, the assessee, who was residing in an excluded area in the Province of Bihar, was served with a notice under Section 22 (2) of the Income-tax Act for furnishing a return in the prescribed form for the year 1940-41 (previous year 1939-40). On the 22nd April, 1940, a notice under Section 22 (1) was published in the press requiring persons generally to submit return in the prescribed form. On the 26th May, 1940, the Governor of Bihar by notification under Section 92 (1) of the Government of India Act, 1935, enacted that the Indian Finance Act, 1940, and some other Income-tax (Amendment) Acts should be deemed to have been applied to the area from the date on which those Acts came into force in other parts of the Province. To remove doubts as to the applicability retrospectively of the Acts mentioned therein the Governor, acting under Section 92 (2) of the Government of India Act, made the Chota Nagpur and Santal Parganas District Validating Regulation, (I of 1941) with the consent of the Governor-General, directing inter alia *that the Indian Finance Act, 1940, should be deemed to have come into force in the area on the 6th April, 1940. The assessee who was assessed to tax on the 9th March, 1941, appealed against the assessment and contended that the assessment was invalid inasmuch as (i) when the notice under Section 22 (2) was served on him the Indian Finance Act, 1940, had not been extended to the area, and the Notification and Regulation could not apply retrospectively to his assessment, (ii) even if they applied the Governor had no power to give a retrospective effect either acting under Section 92 (1) or under 92 (2), and (iii) proper notices had not been issued under sub-sections (1) and (2) of Section 22.*

Held, *(1) that as from the date of the Notification under Section 92 (1) the Indian Finance Act, 1940, applied to the assessment and that therefore the proceedings started thereafter and the assessment which was completed on the 9th March, 1941, were entirely valid ;*

(2) that the assessee could not be allowed to raise the question of the invalidity of the notice under Section 22 (1) when a valid notice under Section 22 (2) had been issued and a return had been filed by him upon that notice;

(3) that as the assessee had appeared and filed the return and as the assessment was completed after the Indian Finance Act, 1940, had been applied to the area, it was not open to him to contend that the notice under Section 22 (2) was invalid because on that date the Indian Finance Act, 1940, had not been applied to the area.

Cases referred to :—

Commissioner of Income-tax *v.* Ekbal & Co. [1945] (13 I.T.R. 154).
Kamakshya Narain Singh *v.* Commissioner of Income-tax [1946] (14 I.T.R. 683).

Reference under Section 66 (1) of the Indian Income-tax Act (XI of 1922) by the Income-tax Appellate Tribunal : (Miscellaneous Judicial Cases Nos. 71 and 82 of 1944).

STATEMENT OF CASE.

"By an application under Section 66 (1) of the Indian Income-tax Act, the applicant asks us to refer the following questions of law that are said to arise out of our order dated 27th July, 1943, in R. A. A. No. 132 Bihar of 1942-43 to the High Court of Judicature at Patna :—

(*a*) Whether the Notification dated 26th May, 1940, read with the Chota Nagpur Division and Santal Parganas District Validating Regulation, 1941, issued by the Governor of Bihar is competent in law to validate the proceedings initiated and completed for the assessment of the applicant under the Indian Income-tax Act, 1922, as amended by the Indian Income-tax (Amendment) Act, 1939, for the assessment year 1940-41?

(*b*) Whether a Hindu undivided family can legally be a partner in a firm?

(*c*) Whether a Hindu undivided family can be assessed for the share in profits received by a member of such family, as partner in a firm?

(*d*) Whether in the circumstances of the case the sum of Rs. 36,310 representing the share of Babu Chatturam in the profits of the firms of Chatturam Darsanram and Bandhanram Guruprasadram has been rightly held by the Tribunal to be assessable as the income of the joint family?

2. The respondent to this application, the Commissioner of Income-tax, Bihar and Orissa, submits that question (*a*) is a question of law and of the questions (*b*), (*c*) and (*d*) raised by the applicant, only question (*d*) arises and therefore both (*a*) and (*d*) may be referred.

3. We find only question (*a*) arises out of our order. As will be shown later, questions (*b*), (*c*) and (*d*) do not arise out of our said order. Therefore question (*a*) alone will be referred to the High Court for their opinion.

4. In the appeal before the Tribunal in respect of the assessment for the year 1940-41 four objections were raised and they were :—

(1) Whether Regulation I issued by the Governor of Bihar applying provisions of Income-tax (Amendment) Act, 1939 (VII of 1939), Income-tax Law Amendment Act, 1940 (XII of 1940), the Excess Profits Tax Act, 1940 (XV of 1940) and the Indian Finance Act, 1940 (XVI of 1940) retrospectively was valid in law to enable an assessment being made for the year 1940-41 in respect of the applicant who is a resident in the Chota Nagpur Division of this Province which is an "excluded area" under Section 92 (2) of the Government of India Act ?

(2) That the order of the Appellate Assistant Commissioner directing the Income-tax Officer to make certain modifications in the assessment made on the applicant consequent on the reassessment ordered by the Appellate Assistant Commissioner of the firm Chatturam Darsanram of which the applicant was a partner was not a proper order under Section 31 of the Indian Income-tax Act ?

(3) That the business carried on by the assessee was not that of the Hindu undivided family and never belonged to any Hindu undivided family.

(4) The allowance received as director's fees by certain members of the family were their personal income and not the income of the family.

The first question raised arises out of the order of the Tribunal in the abovesaid appeal holding that the Governor of a Province has got the plenary powers vested in him to enact an Ordinance with retrospective effect and therefore the Validating Regulation I of 1941 by which the two Acts, the Finance Act of 1940 and the Indian Income-tax (Amendment) Act of 1939, had been applied to the Chota Nagpur Division with retrospective effect is valid.

5. The applicant in this case is a resident of Jhumri Talaiya, a place in the district of Hazaribagh in Chota Nagpur Division. Under the Government of India Act, 1935, this place is an "excluded area." It is common ground that to this "excluded area" only such Acts of the Central Legislature apply as are extended by the Governor of the Province by virtue of power vested in him by Section 92 (1) of the Government of India Act, 1935. The Notification under Section 92 (1) of the Government of India Act, 1935, dated the 26th May, 1940, is as follows :—

"In exercise of the powers conferred by sub-section (1) of Section 92 of the Government of India Act, 1935, the Governor of Bihar is pleased to direct that each of the Acts specified in the Schedule shall be deemed to have been applied to the Santal Parganas and the Chota Nagpur Division with effect retrospectively from the date on which each of the said Acts came into force in other parts of the Province of Bihar."

SCHEDULE.

(1) The Indian Income-tax (Amendment) Act, 1939 (VII of 1939).

(2) The Income-tax Law Amendment Act, 1940 (XII of 1940).

(3) The Excess Profits Tax Act, 1940 (XV of 1940).

(4) The Indian Finance Act, 1940 (XVI of 1940).

Section 92 (2) of the same Act enacted that:—

"The Governor may make regulations for the peace and good government of any area in a Province which is for the time being an excluded area, or a partially excluded area, and any regulations so made may repeal or amend any Act of the Federal Legislature or of the Provincial Legislature, or any existing Indian law, which is for the time being applicable to the area in question."

Later the said Regulation I of 1941 as under was passed:—

"A Regulation to remove doubts as to the operation of certain Acts of the Central Legislature in the partially excluded areas of the Province of Bihar.

Whereas it is expedient to remove doubts as to the operation of certain Acts of the Central Legislature in the partially excluded areas of the Province of Bihar; It is hereby enacted as follows:—

1. (1) This Regulation may be called the Chota Nagpur Division and the Santal Parganas District Validating Regulation, 1941.

(2) It extends to the Chota Nagpur Division and the Santal Parganas District.

(3) It shall come into force at once.

2. (1) Section 1 and Part I of the Indian Income-tax (Amendment) Act, 1939, shall be deemed to have come into force in the area to which this Regulation extends on the 1st day of April 1939.

Provided that sub-clauses (iii) and (iv) of clause (b) of Section 11 shall not be deemed to have taken effect earlier than the 1st day of April 1940.

(2) Part II of the Indian Income-tax (Amendment) Act, 1939, shall be deemed to have come into force in the said area on the date appointed by the Central Government for its coming into force throughout British India generally.

(3) The Income-tax Law Amendment Act, 1940, the Excess Profits Tax Act, 1940, and the Indian Finance Act, 1940, shall be deemed to have come into force in the area to which this Regulation extends on the 26th of March 1940, the 13th day of April 1940, and the 6th day of April 1940, respectively."

The case of the assessee applicant was that the Governor had no powers to apply the four Acts, Indian Income-tax (Amendment) Act, 1939, Income-tax Amendment Act, 1940, Indian Finance Act, 1940, and the Excess Profits Tax Act, 1940, with retrospective effect by any Regulation. The finding of the Tribunal was that he had such powers.

6. This decision was based on the strength of decided English cases mainly the case of *Queen* v. *Burah.*[1] The Tribunal held that under the plenary powers vested in the Governor of a Province, by a Regulation, any Acts that are to be applied under Section 92 (1) of the Government of India Act, 1935, could be applied with retrospective effect.

7. The question raised is if the Governor of a Province has any such plenary powers and the question as raised by the applicant and accepted by the respondent is therefore referred.

8. The questions (*b*) and (*c*) and (*d*) have apparently been raised in regard to the 3rd ground of objection referred to above and disposed of by the Tribunal. The grounds 6 and 7 raised in the appeal before the Tribunal in R. A. A. No. 132 Bihar of 1942-43 were:—

(6) For that the business did not belong to the joint family. There might have been a joint family which the appellants deny—but the business carried on by the appellant never belonged and does not belong to a joint family.

(7) For that movable assets can be held by arrangements by members as their separate property and it would not then be assessable in the hands of the family whether joint or otherwise.

It will be found that these objections did not relate to any particular business of the applicant and the order of the Tribunal in relation to these objections did not discuss any particular business of the applicant. The reference made in the order of the Tribunal to the facts relating to the assessment for the year 1939-40 was in relation to the business of a joint stock company styled Chatturam Horilram Ltd., and the partnership Chatturam Horilram. In the order of the Tribunal any contention of the applicant in regard to the firm Chatturam Darsanram has not been considered as apparently none were urged specifically even at the time of hearing. A reference could be made only of a question of law arising out of an order of the Tribunal in respect of matter disposed of by the Tribunal. As the questions raised (*b*), (*c*) and (*d*) do not arise out of the order of the Tribunal, they cannot be referred. The only question of law that could be referred is in regard to the question of the plenary powers of the Governor and it is referred to their Lordships for their opinion.

Question of law referred:—"Whether the Notification dated 26th May, 1940, read with the Chota Nagpur Division and Santal Parganas District Validating Regulation, 1941, issued by the Governor of Bihar is competent in law to validate the proceedings initiated and completed for the assessment of the applicant under the Indian Income-tax Act, 1922, as amended by the Indian Income-tax (Amendment) Act, 1939, for the assessment year 1940-41."

(1) (1887) 3 App. Cas. 889.

Mahatur Pala and *R. J. Bahadur*, for the assessees.

S. N. Dutta, for the Commissioner.

JUDGMENT.

M. J. C. No. 71 of 1944.

MANOHAR LALL, Ag. C.J.—The Appellate Tribunal at the instance of the assessee has referred to us the following question under Section 66 (1) of the Indian Income-tax Act, 1922 :—

" Whether the Notification dated the 26th May, 1940, read with the Chota Nagpur Division and Santal Parganas District Validating Regulation, 1941, issued by the Governor of Bihar is competent in law to validate the proceedings initiated and completed for the assessment of the applicant under the Indian Income-tax Act, 1922, as amended by the Indian Income-tax (Amendment) Act, 1939, for the assessment year 1940-41."

The facts of this case are somewhat similar to the facts in Miscellaneous Judicial Case No. 130 of 1944* disposed of to-day, but the relevant dates are different.

In this case the assessee has been assessed for the year 1940-41, his previous year being 1939-40.

On the 20th April, 1940, a notice under Section 22 (2) of the Act was served upon the assessee requiring him to furnish a return in the prescribed form. On the 22nd April, 1940, a notice under Section 22 (1) was published in the press requiring persons generally to submit return in the prescribed form. By that time the Indian Finance Act of 1940, which is applicable to this assessment, had not been extended to the excluded area concerning this assessment. On the 26th of May, 1940, the Governor of Bihar by notification under Section 92 (1) of the Government of India Act, 1935, enacted that the Indian Finance Act of 1940 and some other Income-tax Amendment Acts should be deemed to have been applied to the Santal Parganas and the Chota Nagpur Division with effect retrospectively from the date on which these Acts came into force in other parts of the Province of Bihar. To remove doubts as to the applicability retrospectively of the Indian Finance Act and other Acts mentioned therein the Governor of Bihar acting under Section 92 (2) of the Government of India Act made Regulation I of 1941 for the peace and good government of the area in question directing that the Income-tax Law Amendment Act, 1940, the Excess Profits Tax Act, 1940, and the Indian Finance Act, 1940, should be deemed to have come into force in the area to which this Regulation extended on the 26th of March, 1940, the 13th April, 1940, and the 6th of April, 1940, respectively. This was done with the consent of the Governor-General.

The assessment proceedings which had been started as aforesaid were completed on the 9th March, 1941. The appeal of the assessee was

* Since reported as *Kamakshya Narain Singh* v. *Commissioner of Income-tax, Bihar and Orissa* [1946] (14 I.T.R. 683).

dismissed by the Appellate Assistant Commissioner on the 30th December, 1942, and the further appeal to the Tribunal was dismissed on the 27th July, 1943.

We have heard most elaborate and learned arguments by the learned Advocate-General on behalf of the assessee. His contentions may be summarised as follows: (1) The notification and the Regulation cannot apply retrospectively to this assessment on a plain reading of the terms of the two enactments, and (2) even if the Act and the Regulation can be so interpreted, the Governor has no power to give a retrospective effect either acting under Section 92 (1) or acting under Section 92 (2) of the Government of India Act.

In our opinion these contentions are not fit to succeed in this case. It cannot be doubted that from the date of the notification under Section 92 (1) the Indian Finance Act of 1940 must apply to these proceedings. The assessment, therefore, which was actually completed on the 9th March, 1941, was valid as on that date the Indian Finance Act of 1940 was in force in the area in question. It is, therefore, unnecessary to consider the question so ably raised in the argument of the learned Advocate-General except to the extent about to be noticed.

The learned Advocate-General next contended that the notification in question is not expressed to be retrospective in the sense that it does not expressly declare that all assessment proceedings which have already begun (the proceedings in this case began on the 20th April, 1940) must be deemed to have validly begun, and draws attention as an illustration to Ordinance 45 of 1944 by which the Government of India expressly validated the notices which were issued under Section 22 (2). This Ordiance was passed to obviate the difficulties created by the case of *Ekbal* (1945 Income Tax Reports, 154) which decided that such notices were invalid as they allowed the assessee a period of less than 30 days within which the return should be filed. But the short answer to this contention is that no liability to tax attached or attaches before the Finance Act of the relevant year is passed. Therefore, in the present case the liability to tax arose at least on the 26th May, 1940, and the proceedings thereafter were entirely valid. In these circumstances the question whether the notification issued on that date could not be legally made retrospective does not arise for consideration.

It was then argued that even if this was so, the proceedings which were taken before the 26th May, 1940, were invalid. This contention is dealt with below.

The alternative contention of the learned Advocate-General that the Governor acting under Section 92 (2) could not validly pass the Regulation to apply the provisions of the Indian Finance Act retrospectively does not arise for decision in view of the opinion expressed above. But, if it was

necessary to come to a decision, for the reasons given by us while disposing of Miscellaneous Judicial Case No. 130 of 1944*, we would have held that the Governor had power to pass Regulation I of 1941 for the peace and good government of this area, and therefore, the provision in that Regulation that the Indian Finance Act of 1940 shall be deemed to have come into force on the 6th April, 1940, would render the proceedings initiated in this case on the 20th of April, 1940, also valid.

The learned Advocate-General also contended that there was no proper notice issued in this case under Section 22 (1). But a proper notice was admittedly issued under Section 22 (2) on the 20th April, 1940, and in pursuance of that notice the assessee appeared and filed a return. In our opinion the assessee cannot legitimately be allowed to raise the question of the invalidity of the notice under Section 22 (1) when a valid notice under Section 22 (2) has been issued and it is upon that notice that the return was filed by him. The object of the notice under Section 22 (1) is to give a general notice to the public so that they may be ready to file their returns within a certain time. The question may arise for consideration in those cases where no notice has ever been issued under Section 22 (2) of the Act, and the assessee has not filed any return, but that question does not arise in the present case.

Lastly, it was argued that the notice under Section 22 (2) itself must be taken to be invalid because on that date the Indian Finance Act of 1940 had not been applied to this area. Assuming that this argument is correct, the assessee having appeared and filed the return and the assessment having been completed after the Indian Finance Act of 1940 had been applied to this area, the argument of the assessee is wholly untenable on general principles. Take as an illustration a case where an execution is taken out against the judgment-debtor without the issue and service of a notice under Order XXI, Rule 22, of the Code of Civil Procedure. It has been held that the consequent sale of his property is without jurisdiction. But where the judgment-debtor appeared before the sale and raised objections which had been overruled, it has been repeatedly held that the sale cannot be held to be without jurisdiction by reason of the fact that the notice under Order XXI, Rule 22, of the Code of Civil Procedure was not served upon him, the reason being that the object of the notice is to give an opportunity to the judgment-debtor to appear and contest that the decree cannot be put into execution against him on the ground of limitation or on the ground that he had paid off the decretal amount in full or in part or for other valid reasons.

For these reasons the answer to the question referred to us is in the affirmative.

* Since reported as *Kamakshya Narain Singh* v. *Commissioner of Income-tax, Bihar and Orissa* [1946] (14 I.T.R. 683).

In the circumstances each party will bear his own costs in this Court.

M. J. C. No. 82 of 1944.

It was agreed before us that the answer to the question in this case must be the same as the answer the Court will give in M. J. C. No. 71 of 1944. The facts are entirely similar.

For the reasons given while disposing of M. J. C. No. 71 of 1944, the answer to the question below is in the affirmative.

"Whether the Notification dated 26th May, 1940, read with the Chotanagpur Division and Santal Parganas District Validating Regulation, 1941, issued by the Governor of Bihar is competent in law to validate the proceedings initiated and completed for the assessment of the applicants under the Indian Income-tax Act, 1922, as amended by the Indian Income-tax (Amendment) Act 1939, for the assessment year 1940-41.

In the circumstances each party will bear his own costs in this Court.

SINHA, J.—I agree.

DAS, J.—I agree. *References answered in the affirmative.*

[IN THE PATNA HIGH COURT.]

SRI SRI JYOTISHWARI KALIMATA AND OTHERS

v.

COMMISSIONER OF INCOME TAX, BIHAR & ORISSA.

MANOHAR LALL, AG. C. J., and RAY, J. August 21, 1946.

INDIAN INCOME-TAX ACT (XI OF 1922), SECS. 4 (3) (i), 41 (1) FIRST PROVISO—TRUST FOR BENEFIT OF DEITIES—PROPERTIES SET APART TO THREE GROUPS OF DEITIES—FULL DISCRETION TO TRUSTEE TO SPEND INCOME—METHOD OF ASSESSMENT—ASSESSMENT OF TRUSTEE AT MAXIMUM RATE—LEGALITY—NO PROVISION IN DEED TO SPEND INCOME ON CHARITABLE PURPOSES—SUMS SPENT FOR PUBLIC CHARITY—EXEMPTION.

In order to claim exemption for sums spent on charitable purposes by trustees of a private religious trust, the terms of the deed themselves should indicate whether any portion of the trust income enures for the benefit of the public within the meaning of Section 4 (3).

A trust was created by two deeds bearing the same date in favour of certain family deities which were shown in three groups for the purpose of performing the daily worship of the deities and other usual observances. By one of these deeds one set of properties was dedicated in favour of one group, and another set of properties in favour of the second group. By the second deed a third set of properties was dedicated in favour of the third group. Under the deeds the trustee was given full discretion as to the manner and extent in which he should spend the whole or part of the income of a particular year. The balance of the income remaining after

meeting the expenses was to be held by the trustee in trust for the use and benefit of the deities and should form a part of the corpus of the trust properties respectively dedicated to the deities :

Held, (*i*) *that the deities were the owners of the properties, that though their shares were not defined in the deed they were well defined in law and equal and that therefore the income of the trust property in the hands of the trustee was not liable to be assessed at the maximum rate under the first proviso to Section 41 (1) but should be assessed at the rate applicable for the individual income of each of the deities in each group ;*

(*ii*) *that as the deeds did not specifically mention that the trustee should spend part of the income on objects of or for public charity, sums spent by the trustee on charitable purposes should not be excluded under Section 4 (3) (i) for the purposes of determining the income liable to be taxed.*

Cases referred to :—

Gopi *v.* Mussamat Jaldhara [1912] (I.L.R. 33 All. 41).

Jogeswar Narain Deo *v.* Ram Chandra Dutt [1896] (23 Cal. 670 ; 23 I.A. 37 ; 7 Sar. P.C.J. 13 ; 6 M.L.J. 75).

References under Section 66 (1) and (2) of the Indian Income-tax Act (XI of 1922) by the Income-tax Appellate Tribunal: (Miscellaneous Judicial Cases Nos. 41, 54, 55, 56, 57, 58 and 59 of 1944).

The statements of cases in M. J. Case No. 41 of 1944 and M. J. Cases Nos. 54-59 of 1944 were as follows :—

STATEMENT OF CASE.

M. J. Cases Nos. 54 to 59 of 1944.

"By an order in Miscellaneous Judicial Cases Nos. 54 to 59 of 1944, the Honourable High Court of Judicature at Patna, has been pleased to ask us to state a case with reference to the following question of law formulated in 6 applications under Section 66 (2) of the Income-tax Act, filed by the Commissioner of Income-tax, Bihar and Orissa:—

'In the circumstances of the case, is the income of the trust properties in question in the hands of the trustee liable to be assessed at the maximum rate under the first proviso to Section 41 (1) of the Income-tax Act ?'

2. The applicant, the Commissioner of Income-tax, Bihar and Orissa, had filed six applications for reference to the High Court. They were numbered :—

1. 66 R. A. No. 19 (Bihar) of 1943-44;
2. 66 R. A. No. 18 (Bihar) of 1943-44;
3. 66 R. A. No. 20 (Bihar) of 1943-44;
4. 66 R. A. No. 35 (Bihar) of 1943-44;
5. 66 R. A. No. 34 (Bihar) of 1943-44;
6. 66 R. A. No. 36 (Bihar) of 1943-44.

These reference applications related to the following appeals respectively :—

(1) R. A. A. No. 107 (Bihar) of 1942-43.

(*Sri Sri Jyotishwari Kalimata, Sri Sri Jyotishwar, Sri Sri Laxmi Narain Jee, through trustee, Raja Kalyani Prasad Singh Deo of Panchkote* v. *Commissioner of Income-tax, Bihar and Orissa,* relating to 1941-42 assessment);

(2) R. A. A. No. 105 (Bihar) of 1942-43.

(*Sri Sri Jyotishwari Bagalamata, Sri Sri Jyotishwar Shiva, Sri Sri Laxmi Narain Jee, through trustee, Raja Sri Sri Kalyani Prasad Singh Deo Bahadur of Panchkote* v. *Commissioner of Income-tax, Bihar and Orissa*, relating to the assessment for 1941-42);

(3) R. A. A. No. 108 (Bihar) of 1942-43.

(*Sri Sri Rajrajeshwari Mata, Sri Sri Sham Chandra Jee, Sri Sri Raghubar Jee, and Sri Sri Laxmi Narain Jee through trustee, Raja Kalyani Prasad Singh Deo of Panchkote* v. *Commissioner of Income-tax, Bihar and Orissa,* relating to the assessment of 1941-42;

(4) R. A. A. No. 43 (Bihar) of 1944.

(The same appellant and respondent as in (1) above, relating to the assessment for 1940-41);

(5) R. A. A. No. 4 (Bihar) of 1943-44.

(The same appellant and respondent as in (2) above, relating to the assessment for 1940-41);

(6) R. A. A. No. 44 (Bihar) of 1943-44.

(The same appellant and respondent as in (3) above relating to the assessment for 1940-41).

3. The applications under Section 66 (2) by the Commissioner of Income-tax, Bihar and Orissa, which have been numbered Miscellaneous Judicial Cases Nos. 54 to 59, relate respectively to the reference applications, appeals and assessments, as noted in the preceding paragraph.

4. The facts relating to those applications may be stated in brief. Maharajadhiraja Sri Sri Jyoti Prasad Singh Deo of Panchkote executed two trust deeds, both dated 11th September, 1933. By virtue of one of those deeds, two sets of landed properties were dedicated to two groups of Hindu deities, named in groups (1) and (2) in paragraph 2 above, for the purpose of making a permanent provision for the daily Sheba or worship and the observance, performance and celebrations of the usual periodical ceremonies and festivals of the said thakurs; by the other deed another set of properties was similarly dedicated to the deities mentioned in group (3) in paragraph 2 above. The trust deeds do not say anything as to what proportion of income from each set of endowed properties should be spent on each deity named in the group for which the dedication has been made. The learned Appellate Assistant Commissioner says. "I do not find the shares of any of these thakurs at any place determined." The settlor was the first trustee, and

the present opposite party is the son of the author of the trust and the present trustee.

It appears that in the past income from those trust properties used to be included in the assessment of the trustee, namely, the Raja of Panchkote. The original assessment for 1940-41 in each of these cases appears to have been so done. Under Section 34, however, a separate assessment for 1940-41 was later made on each of the three groups of deities through the trustee. The assessments were made at the rates appropriate to the total incomes found. Later on, in view of the order of the Appellate Assistant Commissioner in connection with the appeal relating to the 1941-42 assessment, further Section 34 proceedings were started, and tax was levied at the maximum rate under the 1st proviso to Section 41 (1) of the Act. Assessment for 1941-42 was also made on each of the three groups of deities through the trustee, the rate applied being that applicable to the total income of each of the three groups. Next, in view of the appellate order (already mentioned above) tax was computed at the maximum rate. As regards status, the Income-tax Officer treated the assessee in each case as "Individual" at the 1941-42 assessment. At the two Section 34 assessments for 1940-41 in some cases "I" indicating "Individual" was noted and in some cases nothing was noted. At the appeal stage before the learned Appellate Assistant Commissioner in connection with the 1941-42 assessment, the question of status appears to have been raised, and the appellate Assistant Commissioner said, "I hold that the assessment be made in this case on an 'association of persons.'"

6. Against the appellate orders of the Appellate Assistant Commissioner relating to six appeals of the two years, second appeals were filed before the Tribunal. The appeals were decided by this Bench of the Tribunal, as it was then constituted, by its orders dated 30th June, 1943, and 13th December, 1943. The earlier orders relate to the 1941-42 assessments and the later orders to the assessments for 1940-41. Among other things our predecessors appear to have held that the assessment should not have been made in the status of "association of persons," and that as the trust was in favour of idols specifically named in the trust deed, though their shares were not defined by the trust deed, the law attributed to them equal shares and made them tenants-in-common and not joint tenants; their view was that there should be a separate assessment of the trustee as regards the income of each of the idols (in each group).

7. The respondent in the appeals, namely, the Commissioner of Income-tax, being dissatisfied with this decision of our predecessors, filed six applications for reference to the Honourable High Court under Section 66 (1). In regard to the assessments for 1940-41 the following questions were formulated in the applications under Section 66 (1):—

(i) Whether in the circumstances of the case when the deed of trust does not define any share given to the beneficiaries, *i.e.*, the deities, it can be said that in law the beneficiaries take in equal shares?

(ii) If the answer is in the negative, should not the trustee be assessed under the first proviso to Section 41 (1) of the Income-tax Act at the maximum rate?

In the application for reference relating to the 1941-42 assessments, the above two questions as also the following third question were formulated by the Commissioner :—

(iii) In view of the fact that the terms of the trust deed do not provide for the payments being made to the schools and hospitals, etc., is the Tribunal correct in holding that the sums so paid are excluded under Section 4 (3) (i) of the Income-tax Act for the purpose of determining the income liable to be taxed?

8. Our predecessors were of the opinion that questions Nos. (i) and (ii) formulated by the Commissioner in regard to the six assessments for the two years need not be stated, in view of the fact that although question No. (i) involves a point of law, it was no longer a question of law, having regard to the decision of their Lordships of the Judicial Committee, reported in *Jogeswar Narain Deo* v. *Ram Chandra Dutt*[1]. As question No. (ii) was dependent on the answer of question No. (i) that question was also not considered to be fit for being referred to the High Court. Question No. (iii) formulated by the Commissioner in regard to the 1941-42 assessments has been referred in a somewhat altered form to the Honourable Court in a statement of case marked 66 R. A. Nos. 18, 19 and 20 of 1943-44. We are therefore not stating the facts in regard to this point in this connection.

9. Being again dissatisfied with the order of our predecessors, the Commissioner of Income-tax applied to the Honourable High Court under Section 66 (2), with the result that we have now been asked to state this case. We accordingly refer for the decision of their Lordships the following question of law :—

'In the circumstances of the case is the income of the trust properties in question in the hands of the trustee liable to be assessed at the maximum rate under the first proviso to Section 41 (1) of the Income-tax Act?'

The documents mentioned in the appendix will form part of the paper book. We realise that the trust deeds in question are the most important documents in this connection. These have been copied in full in the paper book in regard to the reference, which is already before their Lordships. At one time we thought that the documents need not be included in the present paper book, but in order to make this paper book self-contained without making it unnecessarily voluminous, we have decided to include

(1) (1896) I.L.R. 23 Cal. 670.

in it only the text of the two deeds, leaving out the schedules of properties in regard to which there is no dispute. The appellate orders in the three cases for each of the years being practically the same, except that the names of the appellants and amounts assessed are different we have considered it sufficient to include in the paper book only one order for each year."

M. J. Case No. 41 of 1944.

"The Commissioner of Income-tax, Bihar and Orissa, has filed these three applications under Section 66 (1) of the Income-tax Act, 1922, asking us to refer the following three questions of law to the High Court of Judicature at Patna. The questions are common in all these three applications :—

(i) Whether in the circumstances of the case when the deed of trust does not define any share given to the beneficiaries, *i.e.*, the deities, it can be said that in law the beneficiaries take in equal shares?

(ii) If the answer to the above question is in the negative, should not the trustee be assessed under the first proviso of Section 41 (1) of the Income-tax Act at the maximum rate?

(iii) In view of the fact that the terms of the trust deed do not provide for the payments being made to the schools and hospitals, etc., is the Tribunal correct in holding that the sums so paid are excluded under Section 4 (3) (i) of the Income-tax Act for the purpose of determining the income liable to be taxed?

2. In his reply to the applications the respondent points out certain clerical mistakes and admits that questions of law do arise. He has framed the questions as follows :—

(i) Whether in the circumstances of the case when the deed of trust does not expressly define the shares given to the named beneficiaries, *i.e.*, the deities, it can be said that in law the beneficiaries take in equal shares.

(ii) If the answer to the above question is in the negative, should not the trustee be assessed to income-tax at the maximum rate?

(iii) In view of the fact that the terms of the trust deed do not specifically provide for payments being made to the schools and hospitals, etc., is the Tribunal correct in holding that the sums so paid are excluded under Section 4 (3) (i) of the Income-tax Act for the purpose of determining the income liable to be taxed?

(iv) Is the income of these private religious trusts exempt from the tax so far as it enures for the benefit of the public and whatever the form of this benefit?

3. We are of opinion that a question of law really arises out of our order mentioned above. We therefore proceed to state the case and will later set out the question that arises in this case.

4. *Facts of the case* :—Maharajadhiraja Sri Sri K. P. Singh of Panchkote created a trust by two deeds both dated 11th September, 1943, in favour of the family deities shown in three groups below :—

(1) (a) Jyotishwari Baglamata.
(b) Jyotishwari Shiva.
(c) Lachminarain Jee.

(2) (a) Jyotishwari Kalimata.
(b) Jyotishwari Shiva.
(c) Lachminarain Jee.

(3) (a) Rajrajeshwari Mata.
(b) Shyamchand Jee.
(c) Raghubar Jee.
(d) Lachminarain Jee.

5. By one deed dated 11th September, 1933, one set of properties was dedicated in favour of group (1) above and another set in favour of group (2), and a third set of properties was dedicated in favour of group (3) by another deed dated 11th September, 1933.

6. The present respondent Raja Sri Sri K. P. Singh is the son of the author of the trust and is the present trustee.

7. For the assessment year 1941-42 the Income-tax Officer treated each of the above three groups as an association of persons and assessed the income of each of these groups from the trust properties dedicated to each in three separate assessments in the hands of Raja Sri Sri K. P. Singh Deo as the trustee at appropriate rates.

8. In an appeal under Section 30 of the Act before the Appellate Assistant Commissioner the assessee appellant raised the following objections amongst others against each of the assessments :—

(1) Income assessed was exempt under Section 4 (3) (i) of the Act.

(2) In the alternative separate assessments should have been made on the income of each of these deities.

(3) There could be no association of persons within the meaning of Section 3 of the Act. The deities must be assessed separately.

(4) The income of the trust properties which was actually spent on charity should not have been made liable to tax within the meaning of Section 4 (3) (i) of the Act.

9. The Appellate Assistant Commissioner decided all of these objections against the assessee appellant. Moreover, he directed the Income-tax Officer to levy the tax on each of these groups at the maximum rate as provided under the first proviso to Section 41 (1) of the Act. The assessee thereupon came up here under Section 33 before us and filed three separate appeals. We, in our order referred to in paragraph 1 above, decided these three appeals under Section 33 in favour of the appellant holding that :—

(1) Whole of the income assessed could not be exempt under Section 4 (3) (i) of the Act. Enquiries should be made whether any part of the income of the private religious trust enured for the benefit of the public. If any part of the income was found to have been spent for the benefit of the public, that part should not attract tax. The part of the income that was spent for the maintenance of a High School, M. E. School, girls' school, charitable dispensary, Sanskrit College and for paying stipend to poor students, should be exempted.

(2) The idols being in the concept of law, juristic persons, were not exempt under the Income-tax law.

(3) The assessment should not have been made as an association of persons.

(4) The trust was in favour of idols specifically mentioned in the trust deed. Though their shares were not defined by the trust deed, the law attributed to them equal shares, and made them tenants-in-common and not joint tenants. Therefore there should be a separate assessment of the trustee as regards the income of such of the idols of which he was the trustee.

10. The Commissioner of Income-tax being dissatisfied with the decision of ours has filed these three applications under Section 66 (1).

11. In view of the elaborate order that has been passed under Section 33 (4), we feel there is no need to recapitulate the reasons in this statement for the decision.

12. We are of opinion that questions Nos. 1 and 2 formulated by the Commissioner of Income-tax, Bihar and Orissa, need not be stated, the reason being that the position in regard to the question No. 1 has been absolutely cleared by their Lordships of the Privy Council in the case referred to in our order under Section 33. Therefore the question, 'whether in the circumstances of the case when the deed of trust does not define any share given to the beneficiaries, *i.e.*, the deities, it can be said that in law the beneficiaries take in equal shares,' is not a question of law but it is only a point of law. It is a settled question of law by their Lordships of the Privy Council and therefore needs no further reference. The question No. 2 also is dependent upon the answer to the question No. 1. Further the answer to the question No. 1 is that, where shares are not defined but by rules of construction beneficiaries take equal shares, proviso to Section 41 (1) cannot apply. In our opinion therefore the only question that arises out of our order is question No. 3 which we shall presently refer. But before that we may draw attention to the relevant paragraphs in the deed of trust.

First document (Raj Rajeswari Mata etc.), page 5 :—

'The trustee shall have full power and authority to apply............... the income..............by making one or more additional items in such manner as he may think proper...........'

Second document (Jyotishwari Kalimata and Baglamata, etc.), page 6:—

'The trustee..............shall have full power and authority to apply ....the income..............by making one or more additional items in such manner as he may think proper...........' The successive trustees have interpreted the above provisions as conferring on them power to apply the income to charitable purposes such as hospital, girls schools, Sanskrit College, etc.

13. As a matter of fact the successive trustees acted on such interpretation and applied a portion of the income to such purposes.

14. A portion of the income having thus, as a matter of fact, been applied to purposes which certainly enured (took effect) for the benefit of the public, the contention of the trustee, on the plain meaning of the excepting proviso to Section 4 (3) (i) of the Income-tax Act, was that this portion at least was exempt from taxation.

15. For the purposes of the reference again it is immaterial whether the trustee is right in his interpretation of the deed. The only question is whether he purported to act in exercise of his power as trustee in applying the money to the purposes specified above.

16. Of course according to the contention of the trustee the word 'enure' in the proviso indicates that it is only the factum of application of the money which is material for the purposes of taxation and therefore it is even immaterial whether or not the deed confers any such power on the trustee. If there were a legal obligation to spend on charity, it would be a charitable trust and would not need the exception for exemption.

17. We accordingly refer under Section 66 of the Act the following question of law to the High Court of Judicature at Patna :—

'Whether the sums spent by trustees on charitable purposes though the purposes are not specifically mentioned in the trust deed, are rightly excluded under Section 4 (3) (i) of the Income-tax Act for the purposes of determining the income liable to be taxed.'"

Dr. D. N. Mitter, Baldeo Sahay and *J. M. Ghosh,* for the assessees.

S. N. Dutta, for the Commissioner.

JUDGMENT.

MANOHAR LALL, AG. C. J.—All these miscellaneous judicial cases were heard together as they involve the construction of the same documents by which certain properties have been dedicated to certain deities. The common question of law which arises in all these cases has been formulated by the Appellate Tribunal as follows :—

"In the circumstances of the case is the income of the trust properties in question in the hands of the trustee liable to be assessed at the maximum rate under the first proviso to Section 41 (1) of the Income-tax Act?"

And in Miscellaneous Judicial Case No. 41 of 1944 which relates to three applications by the Commissioner and numbered 66 R. A. Nos. 18, 19 and 20 of 1943-44 the additional question which has been referred to us is:—

"Whether the sums spent by trustees on charitable purposes though the purposes are not specifically mentioned in the trust deed, are rightly excluded under Section 4 (3) (i) of the Income-tax Act for the purposes of determining the income liable to be taxed."

It is convenient to state the admitted facts.

The Maharajadhiraj Sri Jyoti Prosad Singh Deo Bahadur of Panchkote—hereinafter to be called the trustee—created a trust by two deeds bearing the same date 11th of September, 1933, in favour of certain family deities which are shown in three groups:—

(a) Jyotishwari Baglamata, Jyotishwari Shiva, Lachminarain Jee.

(b) Jyotishwari Kalimata, Jyotishwari Shiva, Lachminarain Jee.

(c) Rajrajeshwari Mata, Shyamchand Jee, Raghubar Jee, Lachminarain Jee.

By one of these deeds dated the 11th September, 1933, one set of properties was dedicated in favour of group (a) as described in Schedule A of the deed and another set of properties in favour of group (b) as described in Schedule B of the same deed. By another deed of the same date another set of properties was dedicated in favour of the deities of group (c).

The assessment was made by the Income-tax Officer in the name of each group of deities through the trustee. Before the Appellate Assistant Commissioner one of the contentions raised was that the trustee holds the property for the benefit of the several idols in each group and since the benefit goes to each of them, separate assessments should have been made by the Income-tax Officer on the income of each of these thakurs and the joint assessment was illegal. The Appellate Assistant Commissioner Mr. Misra examined the contention at great length in an able and careful order and came to the conclusion that "as the beneficiaries had nothing to do with the income or the properties, and the trustee virtually was made the owner, disponer and custodian of the properties and their income, the joint assessment was valid by treating the deities as an 'association of persons.'" He further took the view that the Income-tax Officer should have levied the tax at the maximum rate by virtue of the proviso to Section 41, sub-clause (1), of the Income-tax Act. The Assistant Commissioner in agreement with the Income-tax Officer refused to give a deduction with regard to certain expenses which were claimed as being spent for charitable purposes for the benefit of the public.

The assessee then moved the Appellate Tribunal who came to this conclusion: "The idols are in law juristic persons and the income therefore received by the trustee is received on behalf of such juristic persons...

...... We have pointed out above that the trust is in favour of named deities and though their shares are not defined by the trust deed the law attributes to them equal shares and makes them tenants-in-common and not joint tenants. The case reported in *Jogeswar Narain Deo* v. *Ram Chandra Dutt*[1] is a clear authority for this proposition and in *Gopi* v. *Musammat Jaldhara*[2] the same view was taken following the Privy Council case reported in *Jogeswar Narain Deo* v. *Ram Chandra Dutt*[1].

We therefore hold that each idol should be assessed on that deity's income and the tax should be based upon and recovered from the trustee. The measure of the trustee's liability is the liability of the beneficiary (Section 41) as discussed above. There is no uncertainty as to the shares of the idols. We therefore consider that there should be a separate assessment of the trustee as regards the income of each of the deities of which he is the trustee."

It is argued by the learned standing counsel that upon a true interpretation of the deeds of trust the idols in each group should have been assessed as an "association of individuals." He draws attention to the term in the deeds which directs that the trustee shall in the first place out of the income received by him meet the public charges, cost of litigation and for the preservation and improvement of the trust properties and in the next place pay to the shebait or trustee for the time being as his commission or remuneration and then he is directed to apply and expend the balance of the rents, issues and profits towards the performance of the daily worship of the idol and other usual observances. He also draws attention to the other terms in these deeds which give full discretion to the trustee as to the manner and extent in which he will spend the whole or part of the income of a particular year. He, therefore, submitted that the trustee was the owner of the income as a whole of the properties in each group. The learned standing counsel also suggested in the course of his argument that the property described in the various schedules of the deeds did not vest in the deities but in the trustee.

In our opinion, the terms of the deeds are clear and it must be held that the property is vested in the various deities and not in the trustee even though in the very nature of things the shebait or the trustee must have full control over the income and expenditure—always subject to the directions in the deeds of trust.

Paragraph 7 of the deeds clearly states that the trustee or shebait will make an account of the income and expenditure of the trust properties at the end of the Bengalee month of Chaitra, and if there is balance out of the income after meeting the expenses described then this balance shall be held by him in trust for use and benefit of the deities or thakurs and shall form

(1) (1896) I.L.R. 23 Cal. 670. (2) (1912) I.L.R. 33 All. 41.

a part of the corpus of the trust properties respectively dedicated to the deities or thakurs as aforesaid. It will be observed that the words are "respectively dedicated" and these make it clear that the excess of the income over the expenditure belongs to that deity from whose income the balance is derived and is in the hands of the trustee. Again, the trustee also is empowered to utilise the balance in improving or increasing such trust properties by purchase of other immovable properties, and that the property that is thus acquired shall be deemed to form a part of the corpus of the trust property respectively dedicated to the deities or thakurs as aforesaid. These express words support the view taken by the Tribunal that the deities are the owners of the properties.

The Tribunal have also correctly applied the principle of law laid down in *Jogeshwar Narain Deo* v. *Ram Chandra Dutt*[1]. It must, therefore, be held that the deities in each separate group, should have been assessed separately as their shares are well defined in law.

The facts as regards the second question must now be stated. It is provided in the first part of paragraph 7 of the deeds that "the trustee or shebait shall have full power and authority to apply the additional income derived therefrom to increase the scale of the expenditure or of any one or more of the items of expenditure for such thakurs or deities respectively or by making one or more additional items in such manner as he may think proper." It was contended by the assessee before the Income-tax authorities that deduction should be made out of the assessable income of that amount which was spent in the previous year for some items of public charity. The Appellate Assistant Commissioner came to the conclusion that the trust created by the two deeds was a private religious trust and did not enure for the benefit of the public. The Appellate Tribunal, however, took the view that part of a private religious trust which enures for the benefit of the public should be exempted and an enquiry should, therefore, be directed to find out whether any part of these religious private trusts enures for the benefit of the public. On considering the admitted facts and circumstances they came to the conclusion that those expenses which had been made in the previous years for the benefit of the public such as High School at Kasipur, M. E. Girls School, stipend to poor students, charitable dispensary, Sanskrit College etc., should be exempted from taxation.

The learned standing counsel contends that this view of the Tribunal is wrong. He points out that it is nowhere provided in the trust deeds that the trustee must spend part of the income on objects of or for public charity so that it cannot be held in law that this part of the income enures for the benefit of the public. This argument is correct and must be accepted. The terms of the deeds themselves should indicate whether any portion

(1) (1896) I.L.R. 23 Cal. 670 ; 23 I.A. 37.

of the trust income enures for the benefit of the public within the meaning of Section 4, sub-clause (3), of the Income-tax Act. The only provision in the deeds to which our attention is drawn on behalf of the assessee is to be found in paragraph 7 which I have quoted above. These provisions are not only vague and indefinite but do not contain any direction that any part of the income should or may be spent on specific public charitable purposes. Even though the trustee in a particular year may rightly spend part of the income on public charitable objects, that would amount merely to an application of a part of the income but would not entitle the assessee to claim that that part of the income should be exempt from taxation. Mr. S. N. Dutta further draws attention to these words in the trust deeds: "Any property if thus acquired shall be deemed to form a part of the corpus of the trust property respectively dedicated to the deities or thakurs as aforesaid and the trustee or shebait shall have full power and authority to apply the additional income derived therefrom to increase the scale of the expenditure or of any one or more of the items of expenditure for such thakurs or deities respectively or by making one or more additional items in such manner as he may think proper" and submits that in this case there is no finding that the amount of expenditure which is sought to be exempted came out of the additional income within the meaning of these terms of the trust deeds. If we had taken a different view as to the first part of the question raised, Mr. Dutta would certainly have been entitled to succeed on this part of the argument.

For these reasons the answers to the two questions are as follows:—

(1) In the circumstances of the case, the income of the trust property in question in the hands of the trustee is not liable to be assessed at the maximum rate under the first proviso to Section 41 (1) of the Income-tax Act but should have been assessed at the rate applicable for the individual income of each of the deities in each group.

(2) Sums spent by the trustees on charitable purposes, though the purposes are not specifically mentioned in the trust deed, were wrongly excluded under Section 4 (3) (i) of the Income-tax Act for the purposes of determining the income liable to be taxed.

As the Commissioner of Income-tax has failed substantially in all these references, he must pay cost of the assessees. But as these references were heard together we fix the hearing fee in six cases at Rs. 100, *i.e.*, 54-59 of 1944.

RAY, J.—I agree and have nothing to add.

Reference answered accordingly.

[IN THE BOMBAY HIGH COURT.]

HANMANTRAM RAMNATH

v.

COMMISSIONER OF INCOME TAX, BOMBAY.

SIR LEONARD STONE, C. J., and KANIA, J.

April 2, 1946.

INDIAN INCOME-TAX ACT (XI OF 1922), SECS. 4 (3) (i), 10—EXEMPTIONS—CHARITABLE TRUST—NECESSITY OF DEDICATION OF ASCERTAINED PROPERTY AND DIVESTING OF OWNERSHIP—MERE ENTRIES IN BOOKS OF ACCOUNT, EFFECT OF.

The karta of a joint Hindu family which carried on business made an oral declaration of trust in November 1937 resolving "to set apart a sum of Rs. 2 lacs for religious and charitable purposes and to create a trust of it" and directed that the above sum should be kept credited to the said trust. The amount was not however set apart or credited to any account in the assessee's books on the date of the declaration but the amount was utilised along with other family property in carrying on the family business. In October 1938 an account in the name of the trust was opened and the amount of Rs. 2 lacs was credited to this account. Interest at $4\frac{1}{2}$ per cent. which had accrued from the date of declaration was also credited to this account:

Held, *that, as there was no setting apart of ascertained property and no evidence to show that the settlor had divested himself of the ownership, the entries in the account books did not create a valid trust and the assessee was not entitled to claim a deduction of the interest credited in the books to the trust account from his income under Section 10 of the Indian Income-tax Act.*

Chambers v. *Chambers [1944] (I.L.R. 1944 Mad. 617; 57 L.W. 425; 1944 M.W.N. 567; 48 C.W.N. 621; A.I.R. 1944 P.C. 78; (1944) 2 M.L.J. 29)* referred to.

This reference originally came up for hearing before Sir Leonard Stone, C. J., and Kania, J., on the 21st September, 1944, and the learned Judges sent the reference back to the Tribunal for a further statement of facts: *vide* [1945] (13 I.T.R. 203).

The Tribunal then submitted a further statement of facts.

The facts are fully set out in the Judgment.

C. K. Daphtary, Advocate-General, for the assessee.

M. C. Setalvad, for the Commissioner.

JUDGMENT.

KANIA, J.—This is a reference under Section 66 (1) of the Indian Income-tax Act made by the Income-tax Appellate Tribunal. Having

regard to the way in which the matter of the assessment of the assessee had progressed, considerable confusion had been created, but on the further statement of facts sent by the Tribunal the relevant and material facts are now fairly clear.

The assessee is Rao Bahadur Hanmantram Ramnath of Poona. He is assessed with the status of a joint Hindu family. We are concerned in the present reference with the assessment for the accounting year Samvat 1995 (October 24, 1938, to November 11, 1939). The assessment proceedings were taken in 1940-1941. The assessee, the joint Hindu family, was assessed by the Income-tax Officer on an income of Rs. 86,256 on July 10, 1942. A perusal of the assessment order shows that the assessee claimed that he should be allowed to deduct a sum of Rs. 9,750, being interest which he was liable to pay to "the R. B. Hanmantram Tarachand Charitable Trust Account." In his assessment order the Income-tax Officer has considered the claim as put forth by the assessee. The claim was that the amount being deposited with the joint family firm, interest had become payable on this charitable trust account and therefore the assessee firm should be allowed to deduct the amount as a permissible deduction under Section 10 of the Indian Income-tax Act. The Income-tax Officer rejected this contention because in his opinion no valid trust was created. On appeal to the Appellate Assistant Commissioner, this view was upheld. The matter was then taken by the assessee to the Income-tax Appellate Tribunal. From the record now before this Court, it appears that on behalf of the assessee four affidavits had been filed before the Income-tax Officer in the previous year. No copies of those affidavits were produced before the Income-tax Officer dealing with the assessment under review. The books of account showing how the entries were made and dealt with were perhaps shown to the Income-tax Officer but no extracts were filed up to the time the matter was brought before the Tribunal. The Tribunal therefore dealt with the matter on the meagre materials which were then before it. It decided the question against the assessee. They held that Rao Bahadur Hanmantram did make a declaration creating a trust on November 4, 1937, and on October 23, 1938, an entry crediting the sum of Rs. 2,00,000 to the trust account was made in the assessee's books, but there was nothing to show that there was an actual transfer of assets, which was necessary under Section 6 of the Indian Trusts Act, to constitute a valid trust. They also found that the income as a fact was devoted to charitable and religious purposes. Their conclusion was that the fund which produced the income was not held in trust, on the materials put before them. When the matter came before us, we found that several statements made in the course of that judgment were either not decisions of fact or did not indicate the conclusions as findings of fact. We, therefore, referred back the matter to the

Tribunal under Section 66 (4) of the Indian Income-tax Act.* They have now submitted a full detailed statement containing all the facts and documents which were averred and placed before them. They have submitted for the Court's opinion the question in the following terms:—

"Whether, in the circumstances of the case the sum of Rs. 9,750 is income derived from property held under trust or other legal obligation wholly for religious or charitable purposes within the meaning of Section 4 (3) (i) of the Income-tax Act?"

At the outset it must be pointed out that the question suggested is not the correct question to be answered by the Court. The question submitted can arise, if the trustees who had received this income made a claim that the same was exempted under Section 4 (3) (i) of the Indian Income-tax Act. The facts disclose that the assessee is not a trustee. The assessee has not received this income from the trust funds and has not claimed an exemption under Section 4 (3) (i) of the Act. As shown by the assessment order passed by the Income-tax Officer, the assessee's claim was for an allowance under Section 10 of the Indian Income-tax Act. This defect, however, can be easily put right. The parties appearing before us have conceded that it would be proper for the Court to raise the following question on the facts put before us. The question to be answered will be as follows:—

"Whether the assessee is entitled to claim a reduction of Rs. 9,750 from his income, under the circumstances of the case, under Section 10 of the Income-tax Act?"

To decide this question the Court will have to decide whether this amount was payable by way of interest to a creditor of the assessee. That would give rise to the question, who was the creditor? To answer that question the Court must determine whether there was a valid trust created by Rao Bahadur Hanmantram, because, unless such trust was created, the trustees could not be creditors of the assessee and unless they were creditors, the claim could not be allowed. The question, therefore, reverts back to the discussion contained in the statement of case, *viz.*, whether a valid trust was created by Rao Bahadur Hanmantram?

Although the Indian Trusts Act does not apply to charitable trusts, it is clear that the three certainties there described are required to create a charitable trust. They are: (1) a declaration of trust which is binding on the settlor; (2) setting apart definite property and the settlor depriving himself of the ownership thereof; and (3) a statement of the objects for which the property is thereafter to be held, *i.e.*, the beneficiaries. In the present case there is no dispute about the third. As regards the first also there does not appear to be a serious dispute. The affidavits (copies) were filed in these proceedings and in the course of its judgment the Tribunal has

*See [1945] (13 I.T.R. 203)—Ed.

not stated that it disbelieves the evidence of the deponents. We must therefore proceed on the footing that on November 4, 1937, a declaration of trust as mentioned in the affidavit of Rao Bahadur Hanmantram was made. The following is a material extract from its translation :—

"...... During my illness it was my desire that I should by my own hand give some permanent help to the cause of Religion and Education. Hence I resolved to set apart Rs. two lakhs of my self-acquired estate for the aforesaid religious and charitable purposes and create a trust of it. In accordance therewith, I emphatically declared that Rs. two lakhs out of my estate were in respect of charity, with the consent of the members of my family and in the presence of my circle of friends on the good and auspicious day of the 1st of Kartik Shuddha of Samvat 1994 (November 4, 1937) and I directed that the aforesaid sum should be kept credited to the Rao Bahadur Hanmantram Ramnath (account). I definitely settled that the interest to be realised from the above amount in respect of the charity should be spent for the use of the Dharamshala, hospital, *Anna Chhatra* Education and Hindu orphan persons at Vrindavan and Balaji and for the purpose of carrying on the administration of the said trust accordingly I appointed myself, Hiralal Ramsukh and Shrinivas Hanmantram as Trustees for the time being......"

In addition to the affidavit of Rao Bahadur Hanmantram, affidavits of Shrinivas Hanmantram and Hiralal Ramnath confirming what was stated in the affidavit of Rao Bahadur Hanmantram were also filed. In all these three affidavits it was further stated as follows :—

"As it was unanimously agreed by us all trustees that the said Rs. 2,00,000 should for the present be deposited at interest at the Pedhi of Tarachand Ramnath, the said moneys have been kept at interest at the aforesaid Pedhi."

It is not necessary for us to decide whether the declaration as made was a sufficient and proper declaration, because the question to be considered can be disposed of on the determination of the second point, *viz.*, whether the property is clearly specified and whether the settlor divested himself of beneficial interest in the same.

It appears from the statement of case that on October 23, 1938, certain entries were made in the books of the joint family firm. Before that date, there was in the assessee's ledger an "*Anna Chhatra* account" in Samvat 1994. Rs. 11,639 stood to the credit of that account. There was another account described as the hospital account. In that account Rs. 43,150 stood to its credit. The firm had also a profit and loss account. A sum of Rs. 3,13,607 stood to the credit of that account. On the last day of Samvat 1994 a sum of Rs. 41,000 was debited in the hospital account, a sum of Rs. 11,000 was debited in the *Anna Chhatra* account and a sum of

Rs. 1,48,000 was debited in the profit and loss account. The total of these three, *viz.*, Rs. 2,00,000, was credited in the charitable trust account. At the end of the year interest at the rate of four and a half per cent. was credited and certain amounts were spent on charitable objects. As I have already mentioned before, the Tribunal has noted that the fact of the amounts being spent on charitable objects is not disputed. The question for consideration is whether on these facts the second certainty required to create a trust is found in the transaction.

The Tribunal has found that this certainty is not proved and therefore there was no charitable trust. In our opinion that conclusion is correct. It is not disputed that till the transfer of Rs. 41,000 and Rs. 11,000 from the two accounts, those accounts did not constitute trust accounts. They were only accounts in the books of the assessee. The assessee was entitled to deal with the amounts standing to the credit of those accounts as he thought right, without being liable to account to anyone. By making these three transfer entries, was any property so separated as to prevent the assessee from claiming any beneficial interest therein thereafter? In our opinion the answer to that is in the negative. These are only book entries. It is not shown that on the day the entries were made, a sum of Rs. 2,00,000 was available to the assessee in his safe or in any banking account. We are not concerned with the question whether the firm had credit of Rs. 2,00,000 or had movable property worth Rs. 2,00,000. The question is whether Rs. 2,00,000 in cash were ready as cash of the firm on that day. It was argued that when the settlor and the trustees agreed that the sum in respect of which the settlor created a trust was not necessary to be retained by the trustees but was to be deposited with the assessee's firm at interest, it was not necessary in law for the settlor physically to hand over Rs. 2,00,000 to the trustees and for the trustees to hand back the amount to the assessee in the capacity of a debtor. It is not necessary to consider this argument in the present case, because the initial step of Rs. 2,00,000 being available to the settlor in cash is not established. In the absence of this fact being proved, the entries must be considered only as book entries. The question which arises for determination is whether in the absence of proof of cash being ready, the making of entries in the account books constitutes a separation by the settlor of the trust property from his other property, and discloses that he had deprived himself of the beneficial interest therein, as required by law. In our opinion, the entries mentioned to us do not lead to that conclusion.

On behalf of the Commissioner our attention was drawn to *Chambers v. Chambers*[1]. In that case Mr. Chambers caused entries to be made in the

(1) I.L.R. [1944] Mad. 617.

books of his business, the Chrome Leather Company, crediting Mrs. Chambers, his children by her, and certain other relatives with various sums of money and debiting his capital account in the company's books with those sums. Separate accounts were opened in the respective names showing the sums so credited. In particular in the case of Mrs. Chambers a separate account was opened in the company's books showing ultimately Rs. 2,00,000 to her credit. Before that, on July 25, 1919, Mr. Chambers had written a letter to his company stating *inter alia* as follows:—

"With reference to the amounts at present standing to the credit of my wife and children in your books please make such additions thereto as may be required so that as from April 1st last the capital at their credit in the firm is as follows:—

Mrs. Chambers Rs. 2,00,000. . . .

Please note also that as and from the 1st April last these sums at their respective credits are to bear interest at 6 per cent. payable half-yearly and when the Chrome Leather Company is converted (either with or without the business of Chambers and Co.) into a Limited Liability Company—preference shares at 6 per cent. with interest payable half-yearly are to be issued for the sums at their credit as stated above."

In considering whether this letter, coupled with the entries made as directed therein resulted in producing the second certainty required to create a trust, their Lordships of the Privy Council observed as follows (p. 623):—

"The only question argued before their Lordships was whether a trust in favour of Mrs. Chambers had been effectually constituted .... In India the law of trusts is codified in the Trusts Act (II of 1882) and when the provisions of that Act are consulted, the appellant's case is found to break down at the very threshold. If there is one thing clear it is that there can be no trust unless its subject-matter is clearly ascertainable. Section 8 of the statute declares that 'the subject matter of a trust must be property transferable to the beneficiary.' What then was the subject matter of this alleged trust? Gentle, J., seems to have been of opinion that it was a fund of two lakhs of rupees. But that was not so. No such sum was ever set aside and appropriated by Mr. Chambers as a fund transferable to Mrs. Chambers of which he was to be a trustee with all the consequential obligations of such a position."

In a later part of the same judgment the Board observed as follows (p. 624):—

"There being no ascertained and appropriated trust fund, the case for the constitution of a trust necessarily fails.... The requisites for the constitution of a valid trust are prescribed by Sections 5 and 6 of the Indian Trusts Act."

Their Lordships then set out the terms of those sections and after discussing whether there was a declaration of trust by the letter of Mr. Chambers observed as follows (p. 625):—

"Mr. Chambers never indicated with reasonable certainty by any words or acts an intention on his part thereby to create a trust. His acts were throughout inconsistent with any such intention. As to the trust property, it has already been pointed out by their Lordships that there was no such ascertainment and appropriation as the law requires."

This decision was on the words of the sections of the Indian Trusts Act, which in terms do not apply to charitable trusts. It is, however, equally clear that the necessity of having ascertained property as the subject matter of the trust is none the less in the case of charitable trusts. We therefore agree with the conclusion of the Tribunal that the property not being ascertained and the settlor not being shown to have divested himself of all beneficial interest therein so as to transfer the ownership to the trustees, there is no valid trust in law. If so, there can be no creditor to whom interest is payable and the claim for allowance as made by the assessee was rightly rejected. The answer to the question formulated by us under the circumstances will be in the negative.

In concluding, we must note that the Tribunal has taken considerable pains in setting out in detail the facts as were brought to their notice in this reference. In sending back the reference we had no desire to criticize the manner in which they had held the inquiry in the first instance. We had pointed out that in order to arrive at the conclusion indicated in their judgment it was necessary to set out the facts, as mentioned in our referring judgment. We are glad to note that the Tribunal has followed the lines indicated by us and thus brought to a satisfactory conclusion the somewhat complicated question discussed before them. The assessee will pay the costs of this hearing and also of the first hearing.

Reference answered accordingly.

[IN THE MADRAS HIGH COURT.]

VENKATA SESHAVATHARAM AND OTHERS

v.

CHAPALAMADUGU VENKATA RANGAYYA AND OTHERS.

PATANJALI SASTRI and BELL, JJ. July 8, 1946.

INDIAN INCOME-TAX ACT (XI OF 1922), SEC. 54 (3) (m)—"APPROPRIATE AUTHORITY", MEANING OF—WHETHER INCLUDES "CIVIL COURT"—WHETHER PERSON HAS BEEN ASSESSED TO INCOME-TAX AND THEREFORE NOT

AN AGRICULTURIST—POWER OF HIGH COURT TO CALL DEPARTMENT TO DISCLOSE PARTICULARS—MADRAS AGRICULTURISTS' RELIEF ACT, 1938, SEC. 3 (ii), PROVISO A.

The expression "appropriate authority" in clause (m) of Section 54 (3) of the Indian Income-tax Act, 1922, includes a Civil Court where it is called upon to determine judicially whether a person has or has not been assessed to income-tax in a given year.

The High Court has therefore the power to call upon the Income-tax department to disclose the particulars necessary for determining the issue whether a person has been disqualified from claiming the status of an agriculturist under the Madras Agriculturists' Relief Act, 1938, by reason of his having been assessed to income-tax during the period specified in proviso A to Section 3, clause (ii), of that Act.

Rajoo v. *Palaniappa Chettiar (1940) 2 M.L.J. 817*, referred to.

Appeal against the decree of the District Court of Kistna, at Chilakalapudi, in O. S. No. 30 of 1942, and petition praying that in the circumstances stated in the affidavit filed therewith the High Court will be pleased to call for the original records relating to the assessment to income-tax for 1936-37 of the defendants' family from the Income-tax authorities and print the same if necessary in the said Appeal No. 434 of 1944.

Appeal No. 434 of 1944 and C.M.P. No. 3534 of 1945.

Sir Alladi Krishnaswami Aiyar and *K. Umamaheswaram*, for the appellants.

V. Govindarajachari for *B. Manavala Chowdhury* and *T. K. Subramania Pillai*, for the respondent.

ORDER.

PATANJALI SASTRI, J.—One of the questions raised in this appeal is whether the defendants were agriculturists within the meaning of the Madras Agriculturists' Relief Act, 1938. The plaintiffs who are the appellants here claimed that the defendants were disqualified from claiming the status of an agriculturist under the Act by reason of their having been assessed to income-tax during the period specified in proviso A to Section 3, clause (ii), of the Act, that is to say, in either of the two financial years ending 31st March, 1938. It has been held by this Court in *Rajoo* v. *Palaniappa Chettiar*[1], that the disqualifying assessments must have been made not *for* the two financial years mentioned in the proviso, but must have been made *in* either of those years, as the assessments for any year need not necessarily be made in that year under the Indian Income-tax Act, 1922. In order to establish the disqualification the plaintiffs filed Ex. P-6,

(1) (1940) 2 M.L.J. 817.

a memorandum granted by the Collector of Kistna under Section 26 of the Madras Agriculturists' Relief Act to one Rattayya who was also a creditor of the defendants. This memorandum discloses that Chapalamadugu Rangayya who is admitted to be the manager of the joint family of the defendants was assessed to income-tax for 1936-37 as representing a Hindu undivided family and was not assessed for 1937-38. The memorandum thus throws no light on the point to be determined in the case, for as we have pointed out above what is relevant is not assessment to income-tax *for* the years 1936-37 and 1937-38 but assessment made *in* 1936-37 and 1937-38. Ex. P-18 is another memorandum granted by the same officer on the application of the plaintiffs. It states that Rangayya was *not* assessed to income-tax *for* the two financial years ending 31st March, 1937, and 31st March, 1938. So far as the financial year ending 31st March, 1937, is concerned, this memorandum flatly contradicts the statement in Ex. P-6 that Rangayya was assessed to income-tax for that year. Other similar memoranda granted to the defendants and others have been produced on the defendants' side, Exs. D-5, D-6 and D-14 stating that no assessment in 1936-37 and 1937-38 was made on the said person.

It is suggested by Sir Alladi Krishnaswami Aiyar appearing for the appellants-plaintiffs that in view of the doubt and confusion in which the question relating to the assessment for 1936-37 is involved, we should in the exercise of the powers under Order 41, Rule 27, of the Civil Procedure Code send for the records of the income-tax office concerned to clear up the matter. He relies upon the newly introduced clause (m) of Section 54 (3) of the Indian Income-tax Act as empowering us to call upon the Income-tax department for the production of the records relating to the assessments to income-tax made on Rangayya in the years 1936-37 and 1937-38, the two relevant years for the purposes of the proviso A. It is, however, urged by Mr. Govindarajachari for the respondents that the expression "to the appropriate authority" in clause (m) covers only the Collector acting under Section 26 of the Madras Agriculturists' Relief Act or such other officer as may have occasion to ascertain the particulars referred to in the clause for the purpose of discharging his official duties but not a Civil Court, as a "Civil Court" is referred to as such in clause (d) of Section 54 (3) and not as an "authority." We are unable to accept this narrow construction of the clause. Obviously the clause contemplates the authority concerned calling for such particulars in order to enable it to determine whether a person has or has not been assessed to income-tax in any particular year. Such an issue arises in the present case and the Court has to determine it one way or the other. The wider term "authority" was presumably used with a view to bring also officers such as a Collector acting under Section 26 of the Madras Agriculturists' Relief Act within the purview of the clause.

We cannot agree that the term excludes the Civil Court where it is called upon to determine judicially whether a person has or has not been assessed to income-tax in a given year. We are satisfied that the Court below having the duty of determining whether the defendants were assessed to income-tax in either of the two relevant years had the power to call upon the income-tax department to disclose the particulars necessary for determining that issue, and that we, sitting here in appeal, have also such power.

Mr. Govindarajachari further submitted that, in view of the careless conduct of the appellants, the Court should not call for additional evidence from the income-tax department at this stage in order to assist them to establish their case. As, however, we think that it is not satisfactory to decide the question arising under proviso A in the present state of the record with the two contradictory memoranda Exs. P-6 and P-18 granted by the same public officer with reference to the same matter, and require the additional material which we propose to call for under clause (*b*) of Rule 27 (1) of Order 41 of the Code of Civil Procedure in order to clear the doubt in our minds, no question of the parties' delay or negligence arises. We accordingly call upon the Income-tax Officer, Masulipatam, to produce the original records relating to the assessment to income-tax, if any, made in 1936-37 and 1937-38 on the defendants' family of which Chapalamadugu Rangayya was the manager. The further hearing of this appeal will await the production of those records.

Petition allowed.

[IN THE BOMBAY HIGH COURT.]

COMMISSIONER OF INCOME TAX, BOMBAY

v.

RAIPUR MANUFACTURING CO., LTD.

SIR LEONARD STONE, C. J., and KANIA, J. March 6, 1946.

EXCESS PROFITS TAX ACT (XV OF 1940), SCH. II, R. 1 (1), (2)—COMPUTATION OF CAPITAL—VALUATION OF STOCK DURING STANDARD PERIOD FOR INCOME-TAX PURPOSES—WHETHER BINDING ON EXCESS PROFITS TAX OFFICER—REVALUATION—PERMISSIBILITY—COMPUTATION OF PROFITS—COMMERCIAL PRACTICE.

Where, at the time of making the income-tax assessment during the standard period the Income-tax Officer has accepted the stock valuation made by the assessee on the basis of a fixed rate which was lower than either the cost price or the market price, the Excess Profits Tax Officer, while making the excess profits tax assessments, could not, on a true construction of the provisions of Rule 1 of Schedule II to the Excess Profits Tax Act,

revalue those stocks at cost price for the purpose of making capital computation during the standard period.

The ordinary principles of commercial accounting require that in the profit and loss account of a merchant's or manufacturer's business the values of the stock-in-trade at the beginning and at the end of the period covered by the account should be entered at cost or market price, whichever is the lower, although there is nothing about this in the taxing statutes.

Cases referred to :—

Farmer *v.* Scottish North American Trust Limited ([1912] A.C. 118 ; 5 Tax Cas. 693 ; 105 L.T. 833 ; 28 T.L.R. 142 ; [1910] Sess. Cas. 966).

John Smith & Son *v.* Moore (H. M. Inspector of Taxes) [1921] (12 Tax Cas. 266 ; [1921] 2 A.C. 13 ; 90 L.J.P.C. 149 ; 125 L.T. 481 ; 37 T.L.R. 613).

Russell *v.* Aberdeen Town and County Bank [1888] (13 App. Cas. 418 ; 2 Tax Cas. 321).

Whimster & Co. *v.* Commissioners of Inland Revenue [1925] (12 Tax Cas. 813 ; [1926] Sess. Cas. 20 ; [1925] Sc. L.T. 628).

Reference under Section 66 (1) of the Indian Income-tax Act (XI of 1922) by the Income-tax Appellate Tribunal: (Income-tax Reference No. 9 of 1945).

STATEMENT OF CASE.

" These are three applications by the Commissioner of Income-tax, Bombay, requiring the Tribunal under Section 21 of the Excess Profits Tax Act read with Section 66 (1) of the Income-tax Act to refer to the High Court a question of law arising from the orders of the Tribunal in 14 (1) E. P. T. A. A. No. 60-(Bombay) of 1943-44, 14 (1) E. P. T. A. A. No. 61-(Bombay) of 1943-44 and 14 (1) E.P.T.A.A. No. 62-(Bombay) of 1943-44.

2. While making the excess profits tax assessments for the chargeable accounting periods commencing 1st September 1939 to 31st December 1939, 1st January 1940 to 31st December 1940 and 1st January 1941 to 31st December 1941, the Excess Profits Tax Officer had to compute the capital employed for the business of the assessee during the standard periods and in the course of that computation the question of valuing the business assets was taken up. The relevant provisions relating to valuations of the assets being Rule 1 in Schedule II and sub-rule (1) (*a*) and (2) which are in the following terms were considered :—

'1. (1) Subject to the provisions of this Schedule, the average amount of the capital employed in a business (so far as it does not consist of money) shall be taken to be—

(*a*) so far as it consists of assets acquired by purchase on or after the commencement of the business, the price at which those assets were acquired, subject to the deductions hereafter specified;

(2) The price or value of any assets other than a debt shall be subject to such deductions for depreciation as are necessary to reduce the asset to its written down value and to such other deductions in respect of reduced values of assets as are allowable in computing profits for the purposes of income-tax and, in the case of a debt, the nominal amount of the debt shall be subject to any deduction which has been allowed in respect thereof for income-tax purposes.'

The Excess Profits Tax Officer considered that at the time of making the income-tax assessments, covering the standard periods, the Income-tax Officer had accepted the stock valuations made by the assessee on the basis of a fixed rate which was lower than either market or cost. Upon this consideration, the Excess Profits Tax Officer felt that the deduction in respect of the reduced values allowable to the assessee was nil, since the cost price was below the market price and in his opinion no further deduction was called for in terms of sub-rule (1) (*a*) extracted above. In this view the Excess Profits Tax Officer rejected the valuations made at a fixed rate in income-tax assessments for the standard periods and revalued the stocks on the basis of his own and included his own valuation for the purpose of making the capital computations.

3. Against all the three assessment orders, the assessee preferred appeals to the Appellate Assistant Commissioner, but was unsuccessful. The assessee then came up in appeal to the Tribunal and contended that in terms of sub-rule (2) of Rule 1 in Schedule II to the Excess Profits Tax Act, the Excess Profits Tax Officer was not competent to reject the deductions allowed in respect of the reduced values of assets for the purpose of computing the profits for the income-tax assessments and substitute in their place fresh valuations for the purpose of making capital computations in terms of the provisions extracted above. The Tribunal accepted this contention and held that on a true construction of sub-rule (2) of Rule 1 of Schedule II, the trading stock cannot be valued at any higher figure than at which it was taken for the purposes of computing the profits of the standard periods for income-tax purposes. In our opinion, the following question of law arises from the orders of the Tribunal in 14 (1) E.P.T.A.A. Nos. 60, 61 and 62 Bombay of 1943-44 :—

'Whether upon the facts found by the Tribunal, the Tribunal was correct in holding, upon the true construction of the provisions of Rule 1 of Schedule II to the Excess Profits Tax Act, that the Excess Profits Tax Officer could not value the trading stocks of the assessee company at cost price which was higher than the fixed rate at which the stocks were valued for the purpose of computing the profits of the standard period for income-tax purposes.' "

M. C. Setalvad, for the Commissioner.
Sir Jamshedji Kanga, for the assessee.

JUDGMENT.

STONE, C. J.—This is a reference under the conjoint effect of Section 21 of the Excess Profits Tax Act and Section 66 (1) of the Indian Income-tax Act and relates to the computation for the purposes of excess profits tax to be made in the case of the assessee company.

The first Schedule to the Excess Profits Tax Act contains the rules for the computation of profits for the purpose of excess profits tax and the second Schedule contains rules for computing the average amount of the capital employed in the business concerned. In order to make calculations for excess profits tax in any case four elements have to be considered. First, the profits for what the Act describes as the standard period; secondly, the capital on which such standard period profit was made; thirdly, the profits for the chargeable accounting period; and fourthly, the capital employed in the chargeable accounting period to make those profits; and, it is by comparing the first and the second with the third and the fourth of these calculations that the necessary basis of computation is arrived at. In this reference it is the capital during the standard period, which was the accounting year for income-tax purposes of 1936-37, with which we are concerned, and as formulated by the Appellate Tribunal the question referred to us is:

"Whether upon the facts found by the Tribunal, the Tribunal was correct in holding, upon the true construction of the provisions of Rule 1 of Schedule II to the Excess Profits Tax Act, that the Excess Profits Tax Officer could not value the trading stocks of the assessee company at cost price which was higher than the fixed rate at which the stocks were valued for the purpose of computing the profits of the standard period for income-tax purposes?"

Now this question turns upon the true construction which is to be put upon Rule 1, sub-rule (2), of Schedule II, to the Excess Profits Tax Act. The rule deals with the amount of capital employed in a business and sub-rule (2) is as follows:—

"The price or value of any assets other than a debt shall be subject to such deductions for depreciation as are necessary to reduce the asset to its written down value and to such other deductions in respect of reduced values of assets as are allowable in computing profits for the purposes of income-tax and, in the case of a debt, the nominal amount of the debt shall be subject to any deduction which has been allowed in respect thereof for income-tax purposes."

If the Commissioner is right in this case, the result will be that in order to ascertain the capital employed during the standard period, he will

be able to re-open the accounts on which the assessee was in fact assessed for income-tax purposes in 1936-37, and disturb what was in fact done nearly ten years ago, in spite of the fact that when such assessment was made the power to revise it under the Income-tax Act was one year—now four years under the amendments to the Act made in 1939.

Mr. Setalvad for the Commissioner submits that he is not bound by what the Income-tax Officer in fact did in assessing the profits for the years 1936-37 and that the whole calculation can be re-opened in order to ascertain what ought to have been allowed in 1936-37. This argument is largely based on a comparison of the expressions "as are allowable" with "as has been allowed" contained in the sub-rule in question. The difference in language in the same sub-rule is at first sight significant. But, when the sub-rule is analysed, it will be found that there is a reason for it, since deductions from the assets which can be made under it fall into three categories. First, a deduction for depreciation of assets, other than a debt, as is necessary to reduce the assets to their written down value; secondly, other deductions in respect of reduced values of assets, other than a debt, as are allowable in computing profits for purposes of income-tax; and, thirdly, deductions in respect of a debt being the nominal amount of the debt, subject to any deduction which has been allowed in respect thereof for income-tax purposes. Such an analysis invokes the question as to the right to make the deductions in respect of these three categories. The first category is dependent upon Section 10 (2) (*vi*) of the Indian Income-tax Act and rule 8 of the Income-tax Rules made thereunder, and when that sub-section and that rule are examined, it will be found that what is to be allowed is such percentage on the original cost as is prescribed with respect to the particular commodity and it is Rule 8 which sets out in columns the commodity and fixed percentage. There is nothing discretionary about this, it is all prescribed by a table of percentages. With regard to the second category there is in respect of it no reference in the Income-tax Act, and the right to make the deductions depends on commercial usage in making up accounts. It is in fact the cost price or the market price, whichever is the lower. This being a commercial usage, it is accepted for taxation purposes. That such a commercial usage should be accepted has been held by authority. In the case of *Whimster & Co.* v. *Commissioners of Inland Revenue* [1], the Lord President says this :—

"In computing the balance of profits and gains for the purposes of income-tax, or for the purposes of excess profits duty, two general and fundamental commonplaces have always to be kept in mind."

The Lord President then goes on to describe how the profits in a particular year are made up, and finally he gives this example :—

(1) (1925) 12 Tax Cas. 813, at p. 823.

"For example, the ordinary principles of commercial accounting require that in the profit and loss account of a merchant's or manufacturer's business the values of the stock-in-trade at the beginning and at the end of the period covered by the account should be entered at cost or market price, whichever is the lower; although there is nothing about this in the taxing statutes."

Here again in respect of these deductions it is something fixed and certain and permits of no discretion being exercised by the Income-tax Officer with regard to them. But the third category which is dependent upon Section 10 (2) (*xi*) of the Indian Income-tax Act stands on a wholly different basis. That sub-section deals with the allowance to be made in respect of bad and doubtful debts due to the assessee, and provides that the Income-tax Officer may estimate within a stated limit what is irrecoverable. So that far from it being something fixed or certain this third category depends on the Income-tax Officer's estimate. This is the difference between the first and second categories on the one hand and the third category on the other, and explains the difference in language between the first and second category being "as are allowable" and the third category being "as has been allowed." It does not point to any revaluation being necessary or permissible in the former two categories any more than it is in the latter. I am satisfied that this result can be arrived at not only upon the true construction of the sub-rule of the schedule we are considering, but also as being in accordance with the dictates of commonsense. In my opinion therefore the question should be answered in the affirmative, and the Commissioner pay the costs of this reference.

KANIA, J.—In the statement of case the Tribunal has observed as follows :—

"While making the excess profits tax assessments for the chargeable accounting periods commencing from 1st September 1939 to 31st December 1939 and the years 1940 and 1941 the Excess Profits Tax Officer had to compute the capital employed for the business of the assessee during the standard periods and in the course of that computation the question of valuing the business assets was taken up . . . . He considered that at the time of making the income-tax assessments, covering the standard periods, the Income-tax Officer had accepted the stock valuations made by the assessee on the basis of a fixed rate which was lower than either the market or cost. Upon this consideration, the Excess Profits Tax Officer felt that the deductions in respect of the reduced values allowable to the assessee was nil, since the cost price was below the market price and in his opinion no further deduction was called for in terms of sub-rule (1) (*a*) of the rules of the second Schedule to the Excess Profits Tax Act. In this view he rejected the valuations made at a fixed rate in income-tax assessments for the

standard periods and revalued the stocks on the basis of his own and included his own valuation for the purpose of making the capital computations."

The question thereupon arose whether the Excess Profits Tax Officer had authority to ignore the valuation of the assets and the allowance made by the Income-tax Officer for ascertaining the profits of the assessee company for income-tax purposes for the standard period. The rival contentions are these.

On behalf of the Commissioner it is contended that under Section 4 of the Excess Profits Tax Act the excess profits tax has to be charged on the amount by which the profits during any chargeable accounting year exceed the standard profits. It is therefore necessary to consider what are the standard profits. The answer is in Section 6 (1) of the Excess Profits Tax Act. It is there provided that the standard profits of a business in relation to any chargeable accounting period shall, subject to the provisions of sub-sections (3) and (4), be an amount bearing to the profits of the business during the standard period, if in respect of that business a standard period is available, the same proportion as the chargeable accounting period bears to the standard period. The natural question on this statement of law would be, "But what if the capital differs ?" The answer to that is found in the proviso to that sub-section. It is there provided that if the average amount of capital employed in the business during such chargeable accounting period is greater or less than the average amount of capital employed during the standard period, such amount shall be increased or decreased, as mentioned in the said proviso. In order therefore to determine what tax on excess profits has to be paid by the assessee, the officer has first to ascertain the standard period, the profits of the standard period and the capital employed during that period. He has next to ascertain the profits of the chargeable accounting period and the capital employed during that period. Having got these data the amount of tax has to be worked out as provided in the Act. It is thus necessary to find out the profits and capital as discussed above. For this, provision is made in two separate schedules of the Excess Profits Tax Act. The first Schedule contains rules for the computation of profits for the purposes of excess profits tax, and Rule 1 provides that the profits of a business during the standard period or during any chargeable accounting period shall be separately computed and shall, subject to the provisions of that Schedule, be computed on the principles on which the profits of a business are computed for the purposes of income-tax under Section 10 of the Indian Income-tax Act. There is a proviso to this rule which runs as follows :—

"Provided further that where the profits during any standard period have already been determined for the purpose of an assessment under the Indian Income-tax Act, 1922, such profits as so determined shall, subject to

the adjustments required by this Schedule, be taken as the profits during that period for the purpose of excess profits tax : "

The remaining provisions of the Schedule are not material on the facts of this case. The expression " average amount of capital " is defined in Section 2 (3) of the Act as the average amount of capital employed in any business as computed in accordance with the second Schedule. The material portion of Rule 1 runs as follows :—

"(1) Subject to the provisions of this Schedule, the average amount of the capital employed in a business (so far as it does not consist of money) shall be taken to be—

(*a*) so far as it consists of assets acquired by purchase on or after the commencement of the business, the price at which those assets were acquired, subject to the deductions hereafter specified ;

(*b*) so far as it consists of assets being debts due to the person carrying on the business, the nominal amount of those debts, subject to the said deductions ;

(*c*) so far as it consists of any other assets which have been acquired otherwise than by purchase as aforesaid, the value of the assets when they became assets of the business, subject to the said deductions.

(2) The price or value of any assets other than a debt shall be subject to such deductions for depreciation as are necessary to reduce the asset to its written down value and to such other deductions in respect of reduced values of assets as are allowable in computing profits for the purposes of income-tax, and in the case of a debt, the nominal amount of the debt shall be subject to any deduction which has been allowed in respect thereof for income-tax purposes."

The rest of that rule is not material. On behalf of the Commissioner it is argued that the computation of profits made by the Income-tax Officer may be binding on the Excess Profits Tax Officer to the extent mentioned in the first Schedule, but that has nothing to do with the computation of the average amount of capital for which separate provision is made in the second Schedule. It is contended that when the Excess Profits Tax Officer is making that computation it is his sole absolute right to fix the value of the assets and he is not bound by any valuations or deductions in the values made by the Income-tax Officer in calculating profits for the standard period. To this, it is conceded that there is an exception in respect of a debt, which is allowed for income-tax purposes because of the last words used in the second sub-rule of the first rule of the second Schedule. It is pointed out that in the last part of that sub-rule (relating to deductions in the amount of debt) the expression used is "which *has been* allowed," while the expression used in respect of the reduced values of other assets is " as are *allowable*." It is contended that this distinction is deliberately made by the Legislature.

On the other hand, it is contended on behalf of the assessee that the distinction sought to be made by the use of these two expressions is imaginary. The Court must look at the substance of the legislation and the whole scheme of the Act. It is pointed out that if the Commissioner's argument is accepted, the result will be that while for income-tax purposes the standard profits will be one figure, for the same period it will be a different figure for the excess profits tax. It is contended that this cannot be the scheme of the Act. In this connection strong reliance is placed on the proviso to Rule 1 of the first Schedule where it is provided that the Excess Profits Tax Officer is bound to accept the computation of profits for the standard period as made by the Income-tax Officer. It is argued that the present contention is a device to get round this position, which the taxing authorities cannot legitimately do under the provisions of the Income-tax Act. They find that they are unable to revise or set aside a computation of profits made by the Income-tax Officer for the standard period, and to get round that difficulty this argument is advanced.

The question for determination therefore is, what is the effect of Schedule I, Rule 1, and the proviso quoted above, when read with Schedule II, Rule 1, sub-rule (2)? In my opinion the contention of the Commissioner is wrong. The Excess Profits Tax Act as shown by the preamble itself is a legislation to impose tax on excess profits arising out of certain businesses. The Income-tax Act is the principal legislation which imposes a tax on the income of a person. Section 6 divides the income under five heads which are chargeable to tax. The fourth head is profits and gains of business, profession or vocation. Out of that a certain portion is carved out by the Legislature for the purpose of imposing the excess profits tax. I am unable to accept the contention of the Commissioner that the Excess Profits Tax Act is an entirely independent legislation, which is connected with the Income-tax Act only to the extent it is expressly so stated in the Excess Profits Tax Act. The scheme of the two Acts clearly shows that the Excess Profits Tax Act is a legislation intended to tax the profits of certain businesses in excess of a certain limit as provided in that Act. It is therefore complementary to the Income-tax Act by its very nature. The argument that for considering the average amount of capital employed in the business, the Excess Profits Tax Officer is entitled to completely ignore the provisions of the Income-tax Act, in my opinion, is quite unsound. The scheme appears to me to be simple and clear. The taxing authorities have to ascertain first the standard profits for the standard period. The computation of profits is a recognised method. As observed in *Whimster & Co.* v. *Commissioners of Inland Revenue*[1], the ordinary principles of commercial accounting require that in the profit and loss account of a merchant's or a manufacturer's business the value of the stock-in-trade at

(1) (1925) 12 Tax Cas. 813, at p. 823.

the beginning and at the end of the period covered by the account should be entered at cost or market price, whichever is the lower. This pronouncement recognises that the profits ascertained are a result of the following calculations. The stock in hand at the beginning of the year, plus the circulating assets consisting of goods and materials bought during the year are to be entered on one side of the account. The expenses relating to production and sale of goods have to be entered on that side. In addition to these there may be certain allowances due to wear and tear. On the other side of the account are the sales. Moreover the stock in hand at the end of the year has to be entered. The balance is the profits of the year. This recognised method of computing profits has been accepted as the correct method. The Income-tax Officer, working on this method, arrives at a particular figure as the profits for the standard period. The conclusion, *i.e.*, the amount so determined, is binding on the Excess Profits Tax Officer under Schedule I, Rule 1, proviso. Moreover in accordance with the first rule of the first Schedule it is equally his duty to calculate the profits of the business during the standard period and also during the chargeable accounting period on the principles on which the profits of a business are computed for the purposes of income-tax under Section 10 of the Indian Income-tax Act. This leaves no doubt in my mind that it is not open to the Excess Profits Tax Officer to tinker with any of the figures which have been used for arriving at the profits. The provisions of the second Schedule are to be taken into consideration when he is faced with the question, what increase or decrease in the profits is due to a change in the average capital used in the year? The wording of Rule 1 of Schedule II is very significant. It is to determine the average amount of capital employed in a business. It is stated to consist of three descriptions: (1) Assets acquired by purchase. (2) Assets being debts due to the person carrying on business. This clearly means capital brought by the owner himself, and not any outside debts or funds borrowed by the owner. (3) Assets which have been acquired otherwise than by purchase. If the rule stopped there, the assessee would be in a difficult situation because the law then calculates the amount of capital used by the assessee at cost of assets and his own capital. Clause 2 of that rule therefore makes provision for devaluing those assets. The wording of that clause clearly shows that the method adopted in valuing the assets in the Income-tax Act is recognised as binding and has to be used for the Excess Profits Tax Act also. The first part of that clause deals with the value of assets, other than a debt. It is provided that the same shall be subject to such deductions for depreciation as are necessary to reduce the asset to its "written down value." The term "written down value" is defined in Section 2 (2) of the Excess Profits Tax Act as having the same meaning assigned to that term in sub-section (5) of Section 10

of the Indian Income-tax Act. That sub-section defines "written down value" as follows :—

"Written down value means—(a) in the case of assets acquired in the previous year, the actual cost to the assessee; (b) in the case of assets acquired before the previous year the actual cost to the assessee less all depreciation actually allowed to him under this Act, or any Act repealed thereby, or under executive orders issued when the Indian Income-tax Act, 1886, was in force."

The use of the word "allowed" in this case is very significant. It shows that the expressions "allowable" and "allowed" have the same meaning. It is therefore clear that under the first sentence of Schedule II, Rule 1 (2), the deductions for depreciation are those which are allowable under the Indian Income-tax Act, so as to bring it to its written down value. The second sentence is added by Act XLII of 1940. When this sentence did not exist in the clause it could have been contended that in computing the average amount of capital the only deductions permitted by the rule in that Schedule were the deductions which would come under the expression "written down value" of the Income-tax Act, and the debts which had been allowed to be reduced. No other deductions were permissible. To defeat that argument the Legislature inserted the second sentence in the clause. According to that, such other deductions in respect of reduced values of the assets, as are allowable for the purpose of computing profits for the purposes of income-tax, are to be allowed. The standard for all allowances and deductions therefore remains the standard which is allowed under the Income-tax Act. The last sentence deals with debts and it is clearly connected with Section 10 (2) (*xi*) of the Income-tax Act. The words "which has been allowed" are clearly proper in that case, because a debt is a fixed sum. The question to what extent a deduction is permissible is a matter of inquiry. It has to be ascertained to what extent and within what period it has become a bad debt. The Income-tax Officer has to make these inquiries and allow the necessary deductions under Section 10 of the Income-tax Act. It is therefore clear that all the three provisions contained in Schedule II, Rule 1 (2), relate to and are directly connected with the deductions permissible under the Income-tax Act.

It was argued that it is the duty of the Excess Profits Tax Officer and not of the Income-tax Officer under Schedule II to fix these allowances. This argument is advanced in respect of the deductions or values of the circulating assets which have been valued by the Income-tax Officer for the standard period. My observations are limited to that particular asset which is under discussion in this case. As to the nature of these calculations the observations of Viscount Finlay in *John Smith & Son* v. *Moore* (*H. M. Inspector of Taxes*)[1] may be noticed with advantage. The learned Law Lord

(1) (1921) 12 Tax Cas. 266.

in discussing the nature of capital clearly differentiated between fixed assets and circulating assets. That was a case dealing with excess profits duty sought to be levied on the assessee.

At page 290 it is stated as follows :—

"Lord Johnston stated very clearly the difference between fixed assets and floating assets. The fixed capital assets comprised, he says, land, leases, works and plant. He goes on :—'But there were other assets of a different kind, namely, the floating assets consisting of the stocks of material to be worked up and of the manufactured articles to be sold. With these the appellant company had to commence business, and it was on the turnover of these and their replacement by further material and further manufactured articles that the company was to make its profit or loss.' The whole of the argument which has been addressed to your Lordships on behalf of the Crown on the score of the £30,000 being in the nature of capital expenditure appears to me to ignore the broad distinction between these two classes of assets, the one class consisting of fixed assets, the other consisting of circulating assets which are bought for the very purpose of being re-sold. I desire in this connection to refer to what was said by Lord Atkinson in delivering the judgment which was adopted by the other members of the House in *Farmer* v. *Scottish North American Trust, Limited*[1], and to quote what Lord Herschell said in *Russell* v. *Town and County Bank*[2]. He was dealing with the income-tax, but his language is just as applicable to the excess profits duty :—'The duty is to be charged upon "a sum not less than the full amount of the balance of the profits or gains of the trade, manufacture, adventure, or concern"; and it appears to me that that language implies that for the purpose of arriving at the balance of profits all that expenditure which is necessary for the purpose of earning the receipts must be deducted, otherwise you do not arrive at the balance of profits; indeed, you do not ascertain, and cannot ascertain, whether there is such a thing as a profit or not. The profit of a trade or business is the surplus by which the receipts from the trade or business exceed the expenditure necessary for the purpose of earning those receipts. That seems to me to be the meaning of the word "profits" in relation to any trade or business. Unless and until you have ascertained that there is such a balance, nothing exists to which the name "profits" can be properly applied.'"

Bearing in mind these observations, it is clear that when the word "profits" is used it means the balance of an account in which on one side are entered the opening stock, the cost of goods purchased, the sales expenses, and the expenses of manufacture during the year, and on the other side the price realised by sales and the balance of stock and materials on hand. Each of these figures remains fixed if the profits are to remain what are ascertained as a result of these calculations. If, therefore, in the present

(1) [1912] A.C. 118. (2) (1888) 13 App. Cas. 418, at p. 424.

case, the amount of profits of the standard period is binding on the Excess Profits Tax Officer under the proviso to Schedule I, Rule 1, it is equally clear that the factors which form part of the calculations in arriving at those profits are equally binding on him. In my opinion, an attempt to disturb either the figure of the opening stock or the closing stock would result in the profits being entirely different. If the Excess Profits Tax Officer is precluded from disturbing the profits of the standard period, in my opinion, the wording of Schedule II, Rule 1 (2), does not permit him, in calculating the average amount of capital of the standard period, to disturb the figure of opening or closing stock of that period. By virtue of Schedule I, Rule 1, his authority to fix the deductions in respect of reduced values to that extent is curtailed. This construction reconciles the provisions of Schedule I, Rule 1, and Schedule II, Rule 1.

The proviso to Schedule I, Rule 1, becomes operative when the profits of the standard period have been determined by the Income-tax Officer. In the present case it is common ground that the profits have been so determined. We are not concerned therefore with a case where the Excess Profits Tax Officer has to ascertain for himself the profits of the standard period and the profits of the chargeable accounting period. This aspect is material to be borne in mind because it was argued that Schedule II, Rule 1 (2), contains the provision in respect of debts where an allowance has been made under the Income-tax Act. Apart from this clause there is no provision enabling the Excess Profits Tax Officer to make an allowance in respect of a debt due to the business. The assets of a business would include a debt due to it. If under none of the clauses of Schedule II, Rule 1, the Excess Profits Tax Officer is authorised to decide, to what extent a debt had become bad and should therefore be deducted in arriving at the profits, how should he determine that? As we are not faced with these facts, I do not consider it necessary to discuss the question.

On the admitted facts it is clear that for the standard period the Income-tax Officer had made the assessment of profits under the Income-tax Act in force at the time and the same is binding on the Excess Profits Tax Officer under the proviso to Schedule I, Rule 1, of the Excess Profits Tax Act. I therefore agree that the answer to the question submitted for our opinion by the Tribunal should be as stated in the judgment of the Chief Justice.

Reference answered accordingly.

[IN THE PATNA HIGH COURT.]

COMMISSIONER OF INCOME TAX, BIHAR AND ORISSA

v.

RAJA BAHADUR KAMAKSHYA NARAIN SINGH.

MANOHAR LALL, Ag. C. J., and DAS, J. September 2, 1946.

SALAMI—INCOME OR CAPITAL—QUESTION OF FACT—MINING LEASE—PROSPECTING LICENCE—SALAMI PAID IN SETTLEMENT OF CLAIM THAT EXTENSIONS OF PROSPECTING LICENCES WERE INVALID—SUMS PAID FOR REIMBURSING ASSESSEE IN RESPECT OF CESS PAID ON HIS BEHALF—WHETHER INCOME OR CAPITAL.

The question whether salami *in a particular case is in reality payment of rent in advance and therefore income or is a lump sum payment for transfer of some interest in the property and therefore capital is a question of fact in the main except in so far as it may be urged that on the facts found the inference in law follows that the particular* salami *is income.*

The assessee's predecessor had given to a coal company a prospecting licence in respect of certain coal bearing lands. The licensees were given the option to have a renewal and also to take a coal mining lease on certain terms and conditions. The prospecting licence was subsequently extended for a further period. During the administration of the estate by the Court of Wards when the assessee was a minor, it was again extended four times. When the assessee attained majority he claimed that the licences and the leases under which the company was holding the lands were ultra vires *the Court of Wards. He further claimed that he should be reimbursed in respect of the cess and income-tax which were paid on his behalf to the Government. The assessee and the company entered into a settlement by which the assessee agreed to accept the various prospecting licences, their extensions and the leases, and extended the prospecting licence for a period of seven years on the same terms as were in force on that date. In consideration of the extension of the prospecting licences and validating the leases and the licences and in full settlement of the claim for cesses the company paid to the assessee the following sums: (i) In full settlement of the claim for* salami*; (a) in respect of the extension of the prospecting licences, Rs. 5,25,000 and (b) validating the leases and licences a capital lump sum of Rs. 40,000; (ii) In full settlement of cesses, Rs. 1,76,306.*

Held, *that in the circumstances of the case, the amount of Rs. 5,25,000 received as* salami *and the amount of Rs. 1,76,306 received on account of cess by the assessee were not taxable.*

Cases referred to :—

British South Africa Co. *v.* Commissioner of Income-tax [1946] (14 I.T.R. Suppl. 17 ; 62 T.L.R. 77).

Commissioner of Income-tax, Bihar and Orissa v. Visweshwar Singh [1939] (7 I.T.R. 536; 18 Pat. 805; 1939 P. W.N. 731).

Province of Bihar v. Maharaja Pratap Udai Nath Sahi Deo of Ratugarh [1941] (9 I.T.R. 313; 20 Pat. 699; 194 I.C. 203; A.I.R. 1941 Pat. 289).

Rani Bhubneshwari Kuer v. Commissioner of Income-tax, Bihar and Orissa [1940] (8 I.T.R. 550; 1940 P.W.N. 702; 192 I.C. 316; 22 P.L.T. 670; A.I.R. 1941 Pat. 39).

Reference under Section 66 (1) of the Indian Income-tax Act (XI of 1922) by the Income-tax Appellate Tribunal, Bombay: (Miscellaneous Judicial Case No. 55 of 1945).

STATEMENT OF CASE.

"This is an application under Section 66 (1) of the Indian Income-tax Act made by the Commissioner of Income-tax, Bihar and Orissa, Patna, asking us to refer to the High Court of Judicature at Patna two questions of law said to arise out of the order under Section 33 dated 11th April, 1944, relating to the assessment of Raja Bahadur Kamakshya Narain Singh for the year 1941-42. The Section 33 order in this case was passed by the Calcutta Bench of the Tribunal as it was then constituted.

2. Two sums of Rs. 5,25,000 and Rs. 1,76,306 (among others) were included in the assessment for 1941-42. The sum of Rs. 5,25,000 and a sum of Rs. 1,74,545 were received from Messrs. Anderson Wright & Co., Managing Agents, Bokaro Ramgarh, Ltd., under circumstances which are explained below. The difference between Rs. 1,76,306 and Rs. 1,74,545 is explained in the assessment order as "balances from others." The assessee went up in appeal to the Appellate Assistant Commissioner, Patna, who left both the items of Rs. 5,25,000 and Rs. 1,76,306 out of the assessment. The Income-tax Officer, Special Circle, Patna, thereupon appealed to the Appellate Tribunal against the order of the Appellate Assistant Commissioner, Patna. The Bench of the Tribunal, which heard the appeal, agreed with the conclusions of the learned Appellate Assistant Commissioner. On this the applicant has now come up under Section 66 (1) of the Income-tax Act for a reference to the Honourable High Court.

3. In the year 1907 a prospecting licence was granted to Bokaro Ramgarh Limited by Raja Ram Narain Singh of Ramgarh. This was on 26th November, 1907. The licence was renewed on 6th July, 1911, by the said Raja for a period of seven years from the expiry of the first licence, which was for three years. Raja Ram Narain Singh died on 26th January, 1913, and was succeeded by his minor son Raja Lachhmi Narain Singh. As this Raja was a minor, the Court of Wards took charge of the estate. Raja Lachhmi Narain Singh died on 10th April, 1919, when the present incumbent Raja Bahadur Kamakshya Narain Singh succeeded him. As he too was a minor then, the Court of Wards continued to hold charge of the Ramgarh Estate. The estate was, however, released by the Court of

Wards in 1937 when the respondent personally assumed charge of his Raj. During the period that the Court of Wards administered the estate prospecting licence was renewed four times, on 13th December, 1917, for a period of five years, on 30th March, 1922, for a further period of five years, on 22nd December, 1926, again for a period of five years and on 18th July, 1932, for a period of ten years. It will thus appear that the period of the last renewed licence had not expired when the respondent assumed direct charge of the estate.

4. It is necessary to note here that each prospecting licence was accompanied by a draft mining lease, whereby the respondent agreed to give mining lease during the period of the prospecting licence to the lessee (company) alone at a certain fixed rate. Under the prospecting licence a regular annual recurring payment of a minimum royalty of Rs. 8,000 is to be paid by the company to the respondent; the principal indenture of 1907 provided for an annual rent of Rs. 8,000; this was paid by the company, but when a mining lease was obtained in 1913 this annual rent of Rs. 8,000 merged in royalty on raisings (with the provision of a minimum royalty of Rs. 8,000).

5. The respondent was, after he assumed charge of his estate, advised that under the law governing the Court of Wards it had no power to grant a prospecting licence, and a notice was thereupon served upon the company on 9th March, 1939, intimating that the respondent would not repudiate the mining lease granted by the Court of Wards, but challenged the validity of the prospecting licence issued by the Court of Wards. As such licence was invalid in the eye of law, the respondent proposed to make under-ground settlement of any portion of the Bokaro Ramgarh Coal Fields other than the portion in possession of the company under the mining lease or leases granted in its favour, which the respondent was not repudiating. In the notice the respondent also claimed to be reimbursed in regard to the cesses and income-taxes paid from the date the Court of Wards took over charge of the Ramgarh Estate on behalf of the minor proprietor, together with interest at the rate of 6 per cent. per annum from the date of payment to the date of reimbursement. Ultimately a settlement was arrived at on 10th June, 1940.

Under this settlement the respondent, without admitting the validity of the prospecting licences and leases granted under the terms of the prospecting licences, accepted the licences and leases, as binding on himself and his successors by way of settlement, and waived any claims, which he might have, if the licences and leases were to be held invalid in a Court of law; the company admitted its liability to pay cesses payable by the Raj as lessor from 1932 onwards, and the respondent agreed to accept a sum of Rs. 1,74,545 in full settlement of all claims for cesses and interest thereon up to and including March 1939, he having foregone all claims prior to

1932-33 ; the respondent also agreed to grant the company a further extension of prospecting licence for a period of seven years from 26th November, 1942, on the same terms in all respects as in the licence in force for the time being. In consideration of all this the company agreed to pay to the Raj the following sums:—

(i) In full settlement of the claim for *salami*:

(*a*) in respect of the said extension of the prospecting licence Rs. 5,25,000, and

(*b*) validating the leases and licences a capital sum of Rs. 40,000.

(ii) In full settlement of cesses from 1932-33 up to 1938-39 both years inclusive Rs. 1,74,545. It was further agreed that the deed in respect of the extension of the prospecting licence will be prepared by the solicitors of the company and submitted to the respondent as soon as possible. This document is dated 12th March, 1942.

6. As already mentioned, the Income-tax Officer included the two sums of Rs. 5,25,000 and Rs. 1,76,306 in the assessment of the respondent for 1941-42. He said that the prospecting licence was for a short period, and that only 'exploratory rights' were given, but 'no right to extract coal or alter the existing nature of the property, which remains assessee's own till mining lease is taken.' He went on to observe that 'apparently no question of parting of land or rights thereof over a bomeadi or long periods, as in the case of a mining lease, is involved.' He, therefore, held that the *salami* in the present case is not of the same kind as *salami*, which is now treated as exempt from income-tax assessment on clear authority. He also considered the point that there was some sort of a frequency in the receipt of this *salami* and that 'the same rights are leased and released for definite short terms.' He said that the assessee 'has reserved nothing to himself during the continuance of the prospecting lease by way of his remuneration except the initial payment of Rs. 5,25,000.' In his opinion 'this distinguishes the case from *salami* in other cases where annual rent and royalty are payable in addition..............' He therefore treated this sum of Rs. 5,25,000 as taxable income. As regards the cess recovery of Rs. 1,76,306, the fact that the amount had to be spent by the assessee in payment of cess to Government was not considered by the Income-tax Officer to be of any importance, the destination of income having nothing to do with its assessability or otherwise. He observed: 'Cess for agricultural holdings had been held to be income in the case of *Raja of Ratugarh*[1] and cess for non-agricultural holdings cannot be treated otherwise.'

7. When the case came up before the Appellate Assistant Commissioner, he found that besides the lump sum payment of Rs. 5,25,000, there was a provision for annual payment of Rs. 8,000 as minimum royalty. He also found that the Income-tax Officer was not right in his statement that

(1) [1941] 9 I.T.R. 313.

there was some sort of frequency in the receipt of prospecting *salami*. As regards the cess recovery, the Appellate Assistant Commissioner held 'that the payment is not in the nature of cess as mentioned in the case of *Maharaja of Ratugarh*[1].........' He relied on the Privy Council decision in the case reported as *Bengal Coal Company Ltd.* v. *Sri Janardan Kishore Lal Singh*[2] which said that the liability for payment of cess in that case attached to the occupier of the land under the Bengal Cess Act. In a carefully written judgment, the Appellate Assistant Commissioner has discussed various points and authorities and given his reasons for coming to the conclusion that both these items of receipts should be excluded from the assessment.

8. Next, when the matter was brought up to the Tribunal by the Income-tax Officer, our predecessors, who heard the appeal, for reasons mentioned in their Section 33 order, upheld the decision of the Appellate Assistant Commissioner.

9. On these facts the applicant has asked us to refer the following two questions for the decision of the Hon'ble Court:—

(1) In the circumstances of the case is the amount of Rs. 5,25,000 received as *salami* by the assessee taxable?

(2) In the circumstances of the case is the amount of Rs. 1,76,306 received on account of cess by the assessee taxable?

10. Under Rule 54 of the Appellate Tribunal Rules, the respondent has sent in a written reply to the application for reference. It has been contended that no referable question of law arises out of the appellate order of the Tribunal, both the questions being settled by authority. It must be said that the questions formulated by the applicant are questions of law, and against the respondent's contention that they have ceased to be referable questions of law it has been argued on behalf of the applicant that the points involved in both the questions are slightly different from the points concluded by authorities mentioned by the respondent. The argument may or may not be correct but it is said that the view is arguable. In the circumstances, we think we should not shut out the applicant from obtaining a decision of their Lordships of the Patna High Court directly on the questions formulated.

11. We accordingly refer the following two questions for the decision of the Hon'ble High Court of Judicature at Patna:—

'(1) In the circumstances of the case is the amount of Rs. 5,25,000 received as *salami* by the assessee taxable?

(2) In the circumstances of the case is the amount of Rs. 1,76,306 received on account of cess by the assessee taxable?'"

(1) [1941] 9 I.T.R. 313.

(2) [1938] 6 I.T.R. 632; A.I.R. 1938 P.C. 243.

S. N. Dutta, for the Commissioner.

L. K. Jha, *S. K. Mazumdar* and *Rai Bahadur P. K. Bannerji*, for the assessee.

JUDGMENT.

MANOHAR LALL, AG. C. J.—At the instance of the Commissioner of Income-tax the Appellate Tribunal has referred to us the following questions for decision :—

"(1) In the circumstances of the case is the amount of Rs. 5,25,000 received as *salami* by the assessee taxable?

(2) In the circumstances of the case is the amount of Rs. 1,76,306 received on account of cess by the assessee taxable?"

For the assessment year 1941-42 Raja Bahadur Kamakshya Narain Singh, the assessee, was assessed on a total sum of Rs. 21,65,265. The Income-tax Officer included in this sum Rs. 5,25,000 which was received by the assessee because in his opinion this so called *salami* was nothing but an advance payment of income. He also included a sum of Rs. 1,74,545 (the figure in the question sent to the High Court is 1,76,306 and is agreed to be the correct figure) in the assessable income on the view that this amount was received from the lessees Anderson Wright & Co., and the destination thereof after it was earned was immaterial, namely that it went to reimburse the assessee.

In appeal, the Appellate Assistant Commissioner, Mr. P. K. Sen Gupta, in a careful order came to the conclusion that the amount of *salami* was capital receipt and not taxable. He also came to the same conclusion regarding the amount of cess.

The Income-tax Officer went up in appeal to the Appellate Tribunal contending that the amount received as *salami* and the amount recovered as cess should not have been deducted out of the assessable income. The Appellate Tribunal agreed with the Appellate Assistant Commissioner.

It is now necessary to give the facts shortly in order to trace the origin and nature of the two sums in question which were admittedly received by the assessee in the previous year.

On the 26th of November, 1907, the then Raja Bahadur of Ramgarh gave a prospecting licence to Bokaro Coal Syndicate on receiving a *salami* of Rs. 1,00,000. The period of licence was three years but the licensee was given the option to have a renewal for another two years. The licensee also advanced to the Raja Bahadur a sum of Rs. 7,00,000 by way of loan on certain conditions mentioned in the document. The licensee was at liberty to transfer, assign or sub-let the whole or any part of his rights and interest. By clause 7 the licensee or his nominees were given the right to take a coal mining lease or leases of the whole or any portion of the coal fields covered by the licence upon certain terms, namely *salami* at the rate

of Rs. 10 per standard bigha but not to exceed thirty thousand standar bighas except in certain events. After the expiry of one year from the dat of the licence, a minimum royalty at the rate of Rs. 8,000 per annum wa to be paid by the licensee to the Raja and in case the mining lease o leases were taken by the licensee this minimum royalty was payable s long as the minimum royalty payable under the lease or leases did no reach the figure of Rs. 8,000 per annum. Over and above that a furthe minimum royalty of one rupee per bigha on all lands actually taken up ove and above an area of eight thousand standard bighas was also payable. Th other terms are not important.

On the 6th of September, 1911, the prospecting licence was extende for seven years. The Raja Bahadur died on the 26th of January, 1913, an the Court of Wards assumed charge on behalf of the minor Raja.

On the 13th of December, 1917, the prospecting licence was extende for another five years.

On the 10th of April, 1919, the then Raja Bahadur, who was the fathe of the present assessee, died, and as the assessee was then a minor, th Court of Wards continued to remain in charge of the estate. On the 30t of April, 1922, the licence was extended for another five years, and again o the 22nd of December, 1926, it was extended for another five years. On th 18th of July, 1932, the Court of Wards again extended the licence for period of ten years. The assessee attained his majority on the 10th o August, 1937.

On the 9th of March, 1939, a notice was served on behalf of the asses see upon Anderson Wright & Co., as the Managing Agents of Bokar Limited asserting that under the provisions of the Court of Wards Act i was not within the power of the Court of Wards to grant a prospectin licence and, therefore, the terms of the prospecting licence dated the 18t of July, 1932, the period of which was still unexpired, was not bindin upon the assessee. It was also asserted that the leases which had bee taken in the meanwhile based on the licence were *ultra vires*, and althoug he was legally justified in repudiating these leases but as royalty or mini mum royalty was being paid on those leases, he was not repudiating them Accordingly the assessee informed Anderson Wright & Co., that he wa entitled to make under-ground settlement of any portion of the Bokaro an Ramgarh coal fields other than the portion which was in their possessio under the leases which were not being repudiated. A further claim wa made on behalf of the assessee that he should be reimbursed in respect o the cess and income-tax which were paid on his behalf to the Governmen during the relevant period and he laid a claim at about Rs. 5,00,000 o account of cess and about Rs. 28,00,000 on account of income-tax an super-tax.

The assessee and the coal company entered into a settlement on the 10th of June, 1940, by which the assessee agreed to accept the various prospecting licences and their extensions and the leases which had been granted under the terms of those prospecting licences and extensions. The prospecting licence was extended for a period of seven years from the 26th of November, 1942, on the same terms as were in force on that date. The company agreed to pay to the assessee and the assessee agreed to receive Rs. 1,74,546 in full settlement of all claims for cesses and interest thereon up to and including March, 1939. The fifth term of the settlement may be quoted here :—

"In consideration of the extension of the prospecting licence and validating the leases and the licences and in full settlement of the claim for cesses from 1932-33 to 1938-39 (all claims for prior to 1932-33 having been foregone by you) we agree to pay to the Raj the following sums :—

(i) In full settlement of the claim for *salami* :

(*a*) In respect of the said extension of the prospecting licences Rs. 5,25,000, and

(*b*) Validating the leases and licences a capital lump sum of Rs. 40,000.

(ii) In full settlement of cesses from 1932-33 up to 1938-39 both years inclusive Rs. 1,74,545/14."

It is contended on behalf of the Income-tax Department before us that the sum of Rs. 5,25,000 was nothing less than an advance royalty for seven years at the rate of Rs. 75,000 per annum. This argument is based upon the following observations by Fazl Ali, J. (as he then was), in the case of *Raja Bahadur Visweshwar Singh* [1]: "I concede that in some cases where the rent is ridiculously low and the premium abnormally high, it may be possible to argue that the premium includes advance rent."

In our opinion, the contention raised on behalf of the Income-tax Department is not tenable. The matter was examined at great length by Fazl Ali, J. (as he then was), and by me in the case of *Visweshwar Singh* [1]. In the judgment we examined a number of cases and we came to the conclusion that it would be impossible to lay down any hard and fast rule that a *salami* can in no case be taxable. But the question must depend upon the facts and circumstances of each case. It is unnecessary to embark upon a review of those cases again. This decision was approved by Harries, C.J., and Fazl Ali, J. (as he then was), in *Rani Bhubneshwari Kuer* [2]. The head note correctly states : "It cannot be laid down as a hard and fast rule that *salami* or *nazrana* paid to the landlord for settlement of lands is payment of rent in advance and therefore assessable as income. In some cases it may be payment of rent in advance ; in other cases it might well be a lump sum payment for transfer of the leasehold interest, in which case it will be

(1) [1939] 7 I.T.R. 536. (2) [1940] 8 I.T.R. 550.

a capital receipt. Consequently, whether *salami* is a capital receipt or income can only be determined after a full investigation of all the facts relating to the settlement for which the *salami* or *nazrana* was paid."

A Special Bench of this Court consisting of Harries, C.J., Fazl Ali, J. (as he then was), and myself in the case of *Maharaja Pratap Udai Nath Sahi Deo*[1] came to the same conclusion, namely, "*salami* could not be regarded as income as a matter of law. It may in certain cases be regarded as payment of rent in advance and in such cases it could rightly be regarded as income. Where, however, *salami* could not be regarded as a payment of rent in advance, it could not be regarded as income and would, therefore, not be taxable. *Prima facie*, *salami* is not income, and it is for the Income-tax authorities to show that there do exist facts which would make the *salami* income."

The question raised, therefore, is a question of fact in the main except in so far as it may be urged that on the facts found the inference in law follows that this particular *salami* was income.

The facts which I have set out above are so clear that I have no hesitation in agreeing with the opinion expressed by the Appellate Assistant Commissioner and the Tribunal. It is sufficient to state that here the *salami* was received not on account of any rent due to the assessee but for the settlement of his claim which he had put forward that the licences and the leases under which the coal company was holding the lands were invalid and *ultra vires* of the Court of Wards and, therefore, the assessee was requiring the coal company to vacate the premises. It is surprising that the Commissioner of Income-tax, notwithstanding the clear case law laid down by this Court which appears to have been correctly applied by the Appellate Assistant Commissioner and the Appellate Tribunal to the facts of this case, had thought it fit to come up to this Court.

For these reasons the Appellate Tribunal has correctly treated Rs. 5,25,000 as not being assessable to tax.

Cess: The claim of the Income-tax Commissioner to assess the amount of Rs. 1,76,306 is still more untenable. It will be recalled that this amount was paid to the assessee because in the relevant period the Court of Wards had paid this sum to the Government although the liability to pay this sum was on the coal company. In other words the assessee has been reimbursed to the extent to which he was out of pocket by the omission of the coal company to bear this burden. How can this sum be treated as an income of the assessee in the previous year? The facts have merely to be stated to show that the Appellate Tribunal in agreement with the Appellate Assistant Commissioner came to the correct conclusion.

For these reasons the answers to the two questions are as follows:—

(1) [1941] 9 I.T.R. 313.

Question No. 1—In the circumstances of this case the amount of Rs. 5,25,000 received as *salami* by the assessee is not assessable to taxation.

Question No. 2—In the circumstances of this case the amount of Rs. 1,76,306 received on account of cess by the assessee is not taxable.

The assessee is entitled to the costs in this Court. I would assess the hearing fee at Rs. 500.

DAS, J.—I agree that the answers to both questions should be as proposed by my Lord the Chief Justice. As to the *salami* of Rs. 5,25,000, it was no doubt contended before us that this had nothing to do with the settlement of the claim regarding the previous leases and licences for which a capital lump sum of Rs. 40,000 was paid. It was contended that the *salami* of Rs. 5,25,000 was in respect of the extension of the prospecting licence and that it was really payment of rent in advance. As has been observed by my Lord the Chief Justice, the question if *salami* in a particular case is in reality payment of rent in advance, or is a lump sum payment for transfer of some interest in the property, is a question of fact which can only be determined after a full investigation of all facts relating to the settlement by which the *salami* or *nazrana* was paid. Even if it is conceded that the *salami* in this case was not paid for validating the previous leases and licences, it does not affect the reasoning by which the Appellate Tribunal has come to the conclusion that the *salami* in this case was not payment of rent in advance. The Appellate Tribunal has rightly drawn attention to clause 8 of the main indenture of the 26th of November, 1907, where there is a provision for the payment of a sum of Rs. 8,000 per annum as minimum royalty in addition to the *salami*; it is also stipulated that there will be a further payment of a minimum royalty of one rupee per bigha per annum in respect of each bigha of land held under mining lease in excess of eight thousand bighas, but these payments will be on account of, and not in addition to, the royalties for the time being payable under any mining lease or leases then already taken up by the licensee. These stipulations, which are also incorporated in the indenture, dated the 12th of March, 1942, show that the *salami* paid in this case was not really advance payment of rent. On the contrary, it was a lump sum payment for the rights which were being given to the licensee, namely, the right to prospect the property for a certain number of years and also the right to get mining leases of the whole or such portion or portions of the lands where coal may be found, at some fixed rates; as a matter of fact, draft mining leases formed a part of the indenture of the 26th of November, 1907. In this view of the matter, the *salami* in question is undoubtedly a capital receipt, and is not income.

In the recent case of *British South Africa Co.* v. *Commissioner of Income-tax*[1], their Lordships of the Judicial Committee had to consider

(1) [1946] 14 I.T.R. Suppl. 17; 62 T.L.R. 77.

certain special grants under which exclusive rights were granted to prospect and work any number of mining locations within the area in question, and one of the questions for decision was if certain sums paid in consideration of the grants were "rents, royalties, premiums and profits arising from property" within the meaning of Section 5 (f) of the Income-tax Ordinance of Northern Rhodesia. Their Lordships agreed with the learned Chief Justice of Northern Rhodesia that the sums received were the "fixed price paid on an outright transfer of certain benefits" and could not be regarded as "rents, royalties etc." The same is the case here, and the *salami* paid is the consideration received upon a transfer of certain benefits.

Reference answered accordingly.

[IN THE BOMBAY HIGH COURT.]

S. C. CAMBATTA

v.

COMMISSIONER OF INCOME TAX, BOMBAY.

SIR LEONARD STONE, C. J., and CHAGLA, J. September 6, 1946.

INDIAN INCOME-TAX ACT (XI OF 1922), SEC. 23A—COMPANY—UNDISTRIBUTED PROFITS—ASSESSMENT OF INDIVIDUAL MEMBERS—JOINT SHAREHOLDERS—HUSBAND AND WIFE—METHOD OF ASSESSMENT—ASSESSMENT OF HUSBAND ALONE—LEGALITY.

Where a share stands registered in two or more names, it is the registered holders regarded as an association of persons who must be regarded as the "shareholder" under Section 23A and they must be assessed accordingly.

The assessee and his wife were the joint holders of some shares in a private limited company which did not distribute its profits for the year ending 31st December, 1938, and did not declare any dividend at the annual general meeting held in November, 1939. The articles of association of the company contained a provision under which in the case of joint shareholders the shareholder first named was entitled to exercise the rights of a shareholder. The question was whether in applying the provisions of Section 23A of the Income-tax Act, the assessee, or the assessee and his wife regarded as an association of persons, should be treated as the shareholder liable to be assessed under the section in respect of the dividends on the shares held jointly by the assessee and his wife :

Held, *that Section 23A does not say anything about equities or beneficial ownership, that the provision in the articles that the first named of the joint registered holders was entitled to exercise some of the rights of the shareholder was merely administrative machinery, and that the assessee*

and his wife were assessable under Section 23A in respect of their joint holding like any other association of persons.

Section 23A is a procedural section and not a charging section. It creates a notional income, which is wholly artificial, and which does not in fact exist in the pocket of any shareholder.

Shapurji Pallonji v. Commissioner of Income-tax, Bombay [1945] (13 I.T.R. 113) distinguished.

Reference under Section 66 (2) of the Indian Income-tax Act (XI of 1922) by the Income-tax Appellate Tribunal: (Income-tax Reference No. 3 of 1946).

STATEMENT OF CASE.

"In compliance with their Lordships' order dated March 29, 1945, we are submitting the following case together with the two questions that their Lordships have sent down.

2. The two questions are:—

(1) Whether on the facts proved there was any evidence to support the conclusion that the money paid for the purchase of 1,245 shares belonged solely to the assessee.

(2) Whether in a case in which the provisions of Section 23A have been applied, the proportionate share in the undistributed profits of the company must be taxed in the hands of the shareholder in whose name the shares stood and nobody else.

3. The second question is only indicated in their Lordships' order. We have not been supplied with a copy of the petitioner's application to the High Court. But his learned attorney told us that the question as framed in that application is identical in form and substance with the corresponding question in paragraph 5 of his reference application to the Tribunal. We are accordingly stating it as it occurs therein.

4. The following are the undisputed facts that directly bear on the first of the two questions. They will also help to understand both. We shall presently state the facts that are particularly material to the second.

5. The Hirdagarh Collieries Ltd., is a private limited company with a capital of Rs. 2,50,000 divided into 2,500 shares of Rs. 100 each. Almost the entire capital is held by the assessee and his wife in the shape of 2,495 shares. Ten and five shares out of them are, respectively, held by them in their individual names, and 2,480 shares in their joint names. This block, in turn, consists of two smaller blocks of 1,235 and 1,245 shares. The first was bought in 1931; and the second in 1936, from their former holder Sir Manekji Dadabhai for a sum of Rs. 1,23,500. In this connection, we confess to an error of inadvertence that crept in paragraph 5 of our

judgment. We have there spoken of the whole block of 2,480 shares having been bought in 1936 for a sum of Rs. 1,23,500. The correct facts, however, are that these shares were bought in two blocks as just stated, at a total price of Rs. 2,48,000 in 1931 and 1936, respectively, and, out of them, the block of 1,245 shares was bought for Rs. 1,23,500.

6. In the assessment for the year 1940-41 giving rise to this reference, the Income-tax Officer included in the assessee's total income, a sum of Rs. 81,114 as dividends in respect of the whole block of 2,480 shares. In appeal, the Appellate Assistant Commissioner reduced the amount to Rs. 75,108, after giving a statutory deduction. There is no further dispute as to this figure. But the assessee contended before the Appellate Assistant Commissioner that the proportionate dividends, amounting to Rs. 37,554 in respect of 1,245 shares was the income of his wife and must be excluded from his assessment. He alleged that, although the block stood in their joint names, it was really bought out of her own money. The point appears to have been taken for the first time before the Appellate Assistant Commissioner who, in consequence, caused a further enquiry to be made into it. As a result of it, he dismissed the assessee's contention holding that there was no proof that the assessee's wife had contributed anything to the purchase of 1,245 shares in question. The assessee then appealed to the Tribunal and we took the same view as the Appellate Assistant Commissioner did. We shall presently set out the evidence or material in support of our conclusion. Copies of these orders are annexed as Exhibits A, B and C.

7. The assessee thereupon made an application to the Tribunal asking to refer four questions for their Lordships' opinion, under Section 66 (1) of the Indian Income-tax Act. The Commissioner of Income-tax, Bombay, in his written answer contended that the only question that arose out of our order was a question of fact. We declined to state a case. With regard to questions Nos. 1, 3 and 4 we held that they did not arise out of our order since no such questions with reference to Section 16 (3) of the Indian Income-tax Act had been raised or argued in appeal, nor any findings recorded upon the points. Their Lordships have taken the same view in their order in the assessee's application to them. Then as regards question No. 2, we observed that it did not survive for decision in the view that we took on the question of fact that the assessee was the sole owner of the block of 1,245 shares. The copies of the assessee's application, the Commissioner's reply and our order are, respectively, Exhibits D, E and F.

8. The evidence or material for our finding on the first question consisted of the undisputed facts established on the evidence that the assessee produced before the Income-tax Officer in course of the inquiry that the Appellate Assistant Commissioner had directed. The assessee produced a

deed of trust of 1925, a balance sheet for the year 1922 of a dissolved firm of Messrs. S. C. Cambatta & Co., in which he and his wife had been partners, besides two sets of bank pass books respectively relating to certain trust account and his own personal account. The first two documents were produced for the purpose of showing that the assessee's wife had income of her own from certain trust settlements and deposits of her share of the profits of the firm which had been however dissolved some years ago. The trust bank books showed that the income from the trust used to be credited into the bank. The assessee's bank books of his personal account however, showed that the sums credited to the trust accounts used to be immediately transferred to the assessee's own current account with the bank, and that this state of things continued in the year of account also. None of these facts was disputed before us. On the contrary, in paragraph 5 of his appeal memo to the Tribunal, the assessee admitted that his wife, having no separate bank account of her own, allowed her moneys to be banked in his current account out of the confidence that she reposed in him. Further, admittedly, the assessee had not kept a separate account of his wife's moneys so as to enable one to say that any ascertained sum in his personal bank account belonged to his wife. Thus the undisputed position was that although the wife had money of her own, it had been inseparably mixed with that of her husband in his own bank account. Moreover, the first block of 1,235 shares, although apparently held in the joint names, exclusively belongs to the assessee and that fact has been admitted. He has not taken any objection to the proportionate dividends being included in his assessment. He was unable to show how the two blocks could be distinguished from each other with respect to their ownership. We were asked to presume from the wife's having lodged her own money in her husband's account that she had contributed to the purchase of the shares in question. But that was also the position in 1931 when the other block of 1,235 shares was bought. In our opinion, the assessee was unable to prove affirmatively that the purchase price of 1,245 shares came out of his wife's money.

9. The admitted facts material to the second question are these :—

The amount of Rs. 75,108 represents the dividends in respect of the whole block of 2,480 shares. It was not, however, actually distributed to the assessee and his wife in the year of account, but was deemed to be so distributed in the following circumstances which may be briefly stated. In the assessment of the Hirdagarh Collieries Ltd., for the year 1940-41 the Income-tax Officer found that no profits had been distributed to its shareholders as dividends out of its assessable income up to the end of the sixth month after its accounts of the previous year had been laid before the company in a general meeting. Accordingly, under Section 23A (1) of the Act,

read with its first proviso, the Income-tax Officer made an order that the whole of its undistributed assessable income shall be deemed to have been distributed as dividends amongst the shareholders. As a result, the amount of Rs. 75,108 was deemed to be the dividends proportionate to 2,480 shares held by the assessee and his wife jointly, and came to be included in the assessee's assessment as stated before.

10. Now the assessee's contention as indicated in the second question sent down by their Lordships appears to be that the dividends deemed to have been distributed under the provisions of Section 23A must be assessed in the hands of the shareholder, *i.e.*, an association of persons consisting of the two joint shareholders in this case, and not in his hands as an individual.

11. In connection with this question, we crave their Lordships' leave to say at the outset that the point involved in the question was indicated in paragraph 1 of the assessee's grounds of appeal to the Tribunal, an extract of which we reproduce below :—

'As laid down in the said Section 23A (1) the dividend income in respect of the said 1,245 shares should have been included in the total income of an association of individuals consisting of the assessee and his wife. It was however contended by the assessee that all the said shares belonged to his wife and proofs were produced to show that the said shares were purchased by her in 1936 from Sir Manekji Dadabhai.'

Then paragraphs 2 to 9 deal only with the assessee's contention of his wife's exclusive ownership of shares. A copy of the assessee's grounds of appeal to the Tribunal is annexed as Exhibit G. From all this it can be gathered that the assessee does not appear to have attached importance to the point that he has done before their Lordships. As a matter of fact, the point was not argued in appeal before us, and, in consequence, we did not record any finding on it. But we are now submitting the question in compliance with their Lordships' order. We also think that it is our duty to express our opinion upon it, having had no occasion to do so before.

12. The assessee's contention that the proportionate dividend must be assessed in the hands of joint shareholders as an 'association of persons' appears to be based upon the concluding portion of Section 23A (1) of the Act. After setting out the circumstances in which an Income-tax Officer has to make an order of distribution, the section proceeds to lay down that upon such an order the proportionate share of the dividends of each shareholder shall be included in the total income of such shareholder for the purpose of assessing his total income. But this provision does not speak of either joint shareholders, or an assessment to be made upon them as an association of persons in respect of the dividends of a joint holding. It cannot be the assessee's case that he is not a shareholder at all. The block of 1,245 shares in question is admittedly registered in the joint names of the

two in the company's register. That will be also clear from a list of shareholders that the petitioner, as the managing director of the company, produced before the Income-tax Officer in connection with the company's assessment for 1939-40. A copy of the list is Exhibit H. In our opinion, the term 'shareholder' in Section 23A (1) means any one of the joint shareholders who for the company's purpose is regarded as the shareholder. Now from the list referred to above, it will also appear that the assessee's name stands first in respect of the joint holding. Turning to the articles of association of the Hirdagarh Collieries Ltd., Article 106 provides that where there are joint registered shareholders any one of such persons may vote at any meeting either personally or by proxy in respect of such share as if he were solely entitled thereto; and if more than one of such joint shareholders be present at any meeting personally or by proxy, the one whose name stands first in the register in respect of such share shall alone be entitled to vote. Then Article 171 in respect of payment of dividends is to the effect that in the case of joint holders the first named in the register may be paid the dividend in respect of the joint holding. A copy of the above Articles 106 and 171 of the Articles of Association is Exhibit J.

13. In our opinion, therefore, the term 'shareholder' in Section 23A (1) of the Act means, in the case of joint shareholders, the shareholder whose name stands first in the register in respect of the holding. The assessee whose name stands first must be regarded as the shareholder for the purpose of an assessment in respect of the dividends deemed to be distributed under that section. After all, Section 23A is a section that provides machinery for the purpose of bringing to tax the profits of a company which might otherwise escape assessment by reason of their non-distribution among the shareholders as dividends. It would follow that its provisions must be given effect to consistently with the scheme of taxation in Section 3 which is the main charging section of the Act. The principle of taxation is that the income must be taxed where it is found.

14. The question as it is framed by the assessee is expressed in an abstract form and we feel some difficulty in answering it. Our opinion, therefore, is that in the circumstances of this case the amount of Rs. 37,554 was rightly included in the petitioner's assessment."

Sir Jamshedji Kanga, for the assessee.
M. C. Setalvad, for the Commissioner.

JUDGMENT.

STONE, C. J.—This is a reference under Section 66 (2) of the Indian Income-tax Act, and the questions, which under order of this Court of the 29th of March, 1945, have been submitted by the Tribunal are these :—

(1) Whether on the facts proved there was any evidence to support the conclusion that the money paid for the purchase of 1,245 shares belonged solely to the assessee.

(2) Whether in a case in which the provisions of Section 23A have been applied, the proportionate share in the undistributed profits of the company must be taxed in the hands of the shareholders in whose name the shares stood and nobody else.

Section 23A created what might be described as an artificial income. It is as follows:—

"Where the Income-tax Officer is satisfied that in respect of any previous year the profits and gains distributed as dividends by any company up to the end of the sixth month after its accounts for that previous year are laid before the company in general meeting are less than sixty per cent. of the assessable income of the company of that previous year, (reduced as therein mentioned), he shall, unless he is satisfied that having regard to losses incurred by the company in earlier years or to the smallness of the profit made, the payment of a dividend or a larger dividend than that declared would be unreasonable, make with the previous approval of the Inspecting Assistant Commissioner an order in writing that the undistributed portion of the assessable income of the company of that previous year as computed for income-tax purposes (reduced as therein mentioned) shall be deemed to have been distributed as dividends amongst the shareholders as at the date of the general meeting aforesaid, and thereupon the proportionate share thereof of each shareholder shall be included in the total income of such shareholder for the purpose of assessing his total income."

Only a brief reference need be made to the facts. The company in whose share capital these 1,245 shares stand, is a private limited company with a total share of 2,500 shares of Rs. 100 each, and the assessee and his wife own 2,480 of the total shares. The shares with which we are concerned, *viz.*, the 1,245, were purchased in 1936 in the joint names of the assessee and his wife. The company did not distribute its profits for the year ending the 31st December, 1938, and at the annual general meeting of the company, which was held on the 22nd November, 1939, no dividend was declared. The Tribunal on the question as to the person or persons who is or are assessable to this artificial income under and by virtue of Section 23A has expressed the following opinion:—

"In our opinion, therefore, the term 'shareholder' in Section 23A (1) of the Act means, in the case of joint shareholders, the shareholder whose name stands first in the register in respect of the holding. The assessee whose name stands first must be regarded as the shareholder for the purpose of an assessment in respect of the dividends deemed to be distributed under that section. After all, Section 23A is a section that provides

machinery for the purpose of bringing to tax the profits of a company which might otherwise escape assessment by reason of their non-distribution among the shareholders as dividends. It would follow that its provisions must be given effect to consistently with the scheme of taxation in Section 3 which is the main charging section of the Act. The principle of taxation is that the income must be taxed where it is found.

The question as it is framed by the assessee is expressed in an abstract form and we feel some difficulty in answering it. Our opinion, therefore, is that in the circumstances of this case the amount of Rs. 37,554 was rightly included in the petitioner's assessment."

With respect to the members of the Tribunal, I can find nothing in the section which gives any indication that it is the shareholder whose name stands first in the company's register, who is to be regarded as the person on whom the assessment is to be made. Under the section the undistributed portion of the assessable income of the company shall be deemed to have been distributed as dividend amongst the shareholders as at the date of the general meeting aforesaid, and thereupon the proportionate share thereof of each shareholder shall be included in the total income of such shareholder. Under the General Clauses Act the singular includes the plural, and, therefore, where a share stands registered in two or more names, it is the registered holders, regarded as an association of persons, who must in my opinion be regarded as the "shareholder" and who must be assessed accordingly.

Section 21 of the Indian Companies Act is the section which makes the memorandum and articles of association of a company the contract between the company and its shareholders and it is as follows :—

"The memorandum and articles shall, when registered, bind the company and the members thereof to the same extent as if they respectively had been signed by each member and contained a covenant on the part of each member, his heirs, and legal representatives, to observe all the provisions of the memorandum and of the articles, subject to the provisions of this Act.".

The only relevant articles of the articles of association of this company, with whose undistributed profits this case is concerned, are Articles 106 and 171. Article 106 provides :—

"Where there are joint registered holders of any share any one of such persons may vote at any meeting either personally or by proxy in respect of such shares as if he were solely entitled thereto, and if more than one of such joint holders be present at any meeting personally or by proxy that one of the said persons so present whose name stands first on the register in respect of such share shall alone be entitled to vote in respect thereof."

There follows a provision with regard to executors. Article 171 is :—

"Unless otherwise directed any dividend may be paid by cheque or warrant sent through the post to the registered address of the member or person entitled, or in case of joint holders to any one of them first named in the register in respect of joint holding."

And the rest of that article is not material.

So that it is clear from those articles that the first named of joint registered holders has no special status. In the contract between the company and its members, what is said of him is merely administrative machinery.

It will be convenient in the first place to consider question No. 2, because, if that question be answered by saying that it is the joint holders of these shares who are assessable under Section 23A in respect of their joint holding, like any other association of persons, then question No. 1 will not arise.

Mr. Setalvad in his submissions on behalf of the Commissioner has referred us to the charging sections, *viz.*, Sections 3 and 4 of the Indian Income-tax Act. It is Section 3 which provides that where any Act of the Central Legislature enacts that income-tax shall be charged for any year at any rate or rates, tax at that rate or those rates shall be charged for that year in accordance with, and subject to the provisions of, this Act in respect of the total income of the previous year of every individual, Hindu undivided family, company and local authority, and of every firm and other association of persons or the partners of the firm or members of the association individually.

Section 4 (1) provides that subject to the provisions of this Act, the total income of any previous year of any person includes all income, profits and gains from whatever source derived, and then in lettered sub-paragraphs are the descriptions of the possible sources from which income arises or is to be deemed to arise.

In my opinion, looking at the scheme of the Act, Section 23A is a procedural section and not a charging section. It creates a notional income, which is wholly artificial, and which does not in fact exist in the pocket of any shareholder. Within the terms of that section this artificial income is to be deemed to have been distributed, in this case to the assessee and his wife as the registered holders of the shares. We are not dealing with anything concrete as no distribution has in fact taken place and no shareholder has in fact received any income. Who will ultimately receive these undistributed profits of the company cannot now be predicted, it may depend on survivorship. The section says nothing about equities or beneficial ownership, and nothing would have been easier, if the legislature had so intended, (*sic*) to have provided that the undistributed income of the company should be deemed to be the income of the persons who would be entitled to it beneficially if it had in fact been distributed on the specified date. Accordingly, in my opinion, question No. 2 should be answered in the

affirmative. It is the joint holders, *viz.*, the assessee and his wife who are assessable to tax. Taking that view of the matter, question No. 1 does not arise. In my opinion the Commissioner must pay the costs.

CHAGLA, J.- I agree.

Section 23A deals with the power to assess individual members of certain companies and it provides that the proportionate share of the undistributed dividends of the company of each shareholder shall be included in the total income of such shareholder for the purpose of assessing his total income. Now, the scheme of the Act is fairly plain. Section 3 is the charging section and it charges the total income of the previous year of every individual, Hindu undivided family, company, local authority, and of every firm and other association of persons or the partners of the firm or members of the association individually. But Section 3 does not tell us what the total income of the assessee is. For that you have got to turn to the definition of "total income" contained in Section 2, sub-clause (15), and that sub-clause defines "total income" to be income, profits and gains referred to in sub-section (1) of Section 4 computed in the manner laid down in the Act. Section 4 tells us what the total income of an assessee is to include and we have to turn to the various sections of the Act in order to find out how total income is to be computed.

Now, in my opinion, Section 23A lays down that certain notional income shall form part of the total income of an assessee who answers to the description contained in that section. It provides, as I have pointed out, that in the case of a shareholder of a company whose dividends have not been distributed, but for the purposes of that section shall be deemed to be distributed, in the total income of such shareholder his share of the undistributed dividends shall be included. Mr. Setalvad has argued on behalf of the Commissioner that what we have to determine is whose real income the share of the undistributed dividends is and that although a particular person may stand on the register of a company as a shareholder, still, if it is found on the facts that he is merely a *benamidar* and the shares really belong to someone else, then the income should be deemed to be not of the shareholder but of the real owner. The simple answer to that argument is that Section 23A does not so provide.

We have been asked by Mr. Setalvad, in face of the mandatory provisions of Section 23A that this particular share in the undistributed dividends of the company shall be included in the total income of the shareholder, that we should hold that this should be included not in his total income but in the total income of someone else. In my opinion, it is perfectly clear that under the terms of Section 23A it is only the shareholder who is assessable and no one else. In this case the assessee is not the

shareholder. The shareholders are the assessee and his wife. They are the joint shareholders and within the meaning of Section 23A they constitute the shareholder who is to be assessed in respect of this income.

Now, with great respect to the Tribunal, I fail to find any warrant or authority for the proposition that the term "shareholder" in Section 23A (1) means any one of the joint shareholders who for the company's purpose is regarded as the shareholder. Both the assessee and his wife are on the register of the company as the joint shareholders and I fail to understand how the fact that the company may for the purpose of convenience agree to permit one or the other to exercise some of the rights of the shareholder can affect the question as to who is the shareholder for the purposes of Section 23A of the Act.

In this connection it is material to refer also to Section 16 of the Act. That also is a computing section and sub-clause (3) provides that in computing the total income of any individual for the purpose of assessment, there shall be included so much of the income of a wife or minor child of such individual as arises directly or indirectly in the manner provided in the following sub-clauses. Therefore, that section provides that the income of the wife shall be deemed to be the income of the husband if the conditions laid down in that subclause are complied with. That is a mandatory section and the Income-tax authorities are entitled to include in the total income of the husband the income of the wife, provided, as I said, the conditions laid down in that subsection are complied with. It would not be open to the husband to contend that in fact he is not the real owner of the income but his wife is. Just as that is a mandatory section and provides for computing the total income of the individual under certain circumstances, similarly Section 23A is a mandatory section and lays down rules of computation in computing the total income of the shareholder referred to in that section.

Mr. Setalvad has relied on a decision of our Court, *Shapurji Pallonji* v. *Commissioner of Income-tax, Bombay*[1]. In that case one S. P. Mistry and P. P. Mistry were two of the partners in a partnership firm. That partnership was registered under Section 26A of the Income-tax Act. In that registration the father was shown as having 6 as. 8 ps. share and the son as having 4 as. share. In the assessment the taxing authorities came to the conclusion that the son was merely a *benamidar* and that the 4 as. share given to the son really belonged to the father, whereupon under Section 23, sub-clause (5) (*a*), they assessed the father in his individual assessment not in respect of the 6 as. 8 ps. share but in respect of the whole of the 10 as. 8 ps. share. It was thereupon contended that the Income-tax authorities having registered the firm and the firm continuing to be registered under Section 26A it was not open to the taxing authorities to assess the father on

(1) [1945] 13 I.T.R. 113.

the basis that the share was 10 as. 8 ps., when in the partnership deed which was registered with the authorities it was shown that his share was only 6 as. 8 ps. That contention was rejected by a Division Bench consisting of the learned Chief Justice and Mr. Justice Kania.

Now, with respect to Mr. Setalvad, I fail to see the analogy between that case and the case we have before us. Section 23 (5) provides that in the case of a registered firm, the sum payable by the firm itself shall not be determined but the total income of each partner of the firm including therein his share of its income, profits and gains of the previous year, shall be assessed and the sum payable by him on the basis of such assessment shall be determined. Therefore in the case of an individual partner, in his total assessment is to be included his share in the income, profits and gains of the partnership. There was nothing to preclude the taxing authorities from determining what the real share of the individual partner was in the income, profits and gains of the previous year. Although the partnership deed stated that his real share was only 6 as. 8 ps., the taxing authorities came to the conclusion that in fact the real share was 10 as. 8 ps. The learned Chief Justice held in his judgment that the taxing authorities were not estopped by Section 26A and Mr. Justice Kania decided the case on another ground, *viz.*, that Section 23 (5) (*a*) did not provide in terms for the assessment of the partners in their names according to the instrument registered with the Income-tax Office. There is, it need hardly be pointed out, nothing mandatory in Section 23 (5) (*a*) which lays down that in the case of an assessment of an individual partner in his total income shall be included his share in the income, profits and gains of the firm according to the tenor of the partnership deed registered with the Income-tax authorities. If we turn to Section 23A, as I have pointed out more than once, you have a mandatory provision saying what should be included in the total income of a shareholder of certain companies.

In the circumstances, I feel that the taxing authorities are wrong in assessing the share of the undistributed profits as the income of the assessee. He is not the shareholder and under Section 23A this income can only be assessed as that of the shareholder, and that shareholder is not the assessee but the assessee and his wife who are the joint holders of the shares in question. I, therefore, agree with the learned Chief Justice that the question referred to us should be answered in the manner suggested by him.

Reference answered accordingly.

[IN THE MADRAS HIGH COURT.]

COMMISSIONER OF INCOME TAX, MADRAS

v.

RM. AR. AR. RM. ARUNACHALAM CHETTIAR (Estate of).

SIR LIONEL LEACH, C.J., and PATANJALI SASTRI, J.

August 16, 1946.

INDIAN INCOME-TAX ACT (XI OF 1922), SEC. 4 (1) (*b*) (*iii*) & THIRD PROVISO—FOREIGN INCOME—EXEMPTION OF RS. 4,500—REMITTANCE OF EXEMPTED INCOME IN SUBSEQUENT YEAR—ASSESSABILITY—APPLICABILITY AND SCOPE OF SEC. 4 (1) (*b*) (*iii*) AND THIRD PROVISO.

Under the third proviso to Section 4 (1) of the Indian Income-tax Act if the amount of foreign income of the year of account exceeds the amount of foreign income brought into British India in that year, the assessee need not pay tax on that part of his foreign income which is not brought into British India, *if such income does not exceed Rs. 4,500. The proviso does not mean that when the income thus exempted is brought to British India in a subsequent year, it shall not be taxable inasmuch as there is nothing in this proviso which detracts from the effect of clause (iii) of Section 4 (1) (b) under which if income which has accrued outside British India before the year of account is brought into British India in that year, it is subject to the tax.*

Case referred to the High Court by the Income-tax Appellate Tribunal, Madras Bench, under Section 66 (1) of the Income-tax Act (XI of 1922) as amended by Section 92 of the Income-tax (Amendment) Act (VII of 1939) in 66 R. A. No. 25-Madras of 1944-45 on its file for decision on the following question of law, *viz.*,

"Whether in the circumstances of the case the sum of Rs. 3,459 was rightly assessed for the assessment year 1941-42?"

Case referred No. 18 of 1945.

STATEMENT OF CASE.

"This application for reference is made by the Commissioner of Income-tax, Madras, for the purpose of referring the following question of law for the opinion of the Hon'ble High Court at Madras :—

'Whether in the circumstances of the case the Bench was correct in holding that the sum of Rs. 3,459 in question was not assessable for the year 1941-42?'

2. The application arises out of the Tribunal's order dated 26th April, 1944, in R. A. A. No. 249-(Madras) of 1942-43. The facts of the case are as under :—

The respondent had a business in Rangoon amongst other places. The accrued income from the Rangoon business for the accounting year ending 31st March, 1941, was Rs. 42,051. The remittances from Rangoon during that year exceeded this amount, and the Income-tax Officer in his assessment order has apportioned these remittances into three figures as under:—

(1) Rs. 42,051 remittances out of accrued income of the 'previous year.'

(2) Rs. 3,459 remittances out of unassessed profits of older years.

(3) Rs. 1,80,469 remittances out of assessed profits of older years and out of capital.

It is in connection with the second item of Rs. 3,459 that a dispute had arisen. It was contended on behalf of the respondent that the sum of Rs. 3,459 should not have been assessed as remittance of older profits from Rangoon under Section 4 (1) (*b*) (*iii*) of the Income-tax Act, and that such profits were exempted from tax as a result of the operation of the third proviso to Section 4 (1) at the time assessment for previous years was made. The proviso referred to above reads as under :—

'Provided further that if in any year the amount of income accruing or arising without British India exceeds the amount brought into British India in that year, there shall not be included in the assessment of the income of that year so much of such excess as does not exceed Rs. 4,500.'

The Tribunal after consideration of this point decided it in favour of the respondent and its reasons for so doing are given at length in paragraphs 6 to 8 of its order under Section 33 (4) (*vide* Exhibit T. E.). In coming to that decision, the Tribunal ultimately observed that in its view the sum of Rs. 3,459 in respect of the Rangoon business was not covered by the provisions of Section 4 (1) (*b*) (*iii*) and, therefore, could not be treated as a remittance out of the older profits that was liable to be assessed.

3. The respondent in his written reply dated 15th January, 1945, (Exhibit T. G.) has suggested a different question of law which runs as under :—

'Whether the amounts of foreign income of the respondent for the years 1938-39 and 1939-40 which were subject of assessment for the years 1939-40 and 1940-41, but exempted from tax by virtue of the provisions contained in the third proviso to Section 4 (1) of the Income-tax Amendment Act of 1939, can be legally assessed in a subsequent year when such sums were received in British India.'

We do not consider either of these questions as quite appropriate, and would, therefore, refer the following question of law for the opinion of the Hon'ble High Court :—

'Whether in the circumstances of the case the sum of Rs. 3,459 was rightly assessed for the assessment year 1941-42 ?' "

C. S. Rama Rao Sahib, for the Commissioner.

A. C. Sampath Ayyangar, for the assessee.

Judgment of the Court was delivered by the Hon'ble the Chief Justice.

JUDGMENT.

This is a reference made at the instance of the Commissioner of Income-tax by the Income-tax Appellate Tribunal, Madras branch, under Section 66 (1) of the Income-tax Act. The assessees are the receivers of the estate of a deceased Nattukottai Chettiar named Rm. Ar. Ar. Rm. Arunachalam Chettiar. Before his death the deceased had carried on a money-lending business in Rangoon and after his death it was continued by the receivers of his estate. The income from the Rangoon business for the year of account 1940-41 was returned at Rs. 42,051. The remittances from Rangoon during that year far exceeded this sum. The Income-tax Officer placed the remittances into three categories. The first category consisted of remittances out of the income of the two previous years. The amount was Rs. 42,051. The second category represented remittances out of unassessed profits of former years. The amount here was Rs. 3,459. The third category represented remittances out of assessed profits of older years and out of capital, the amount being Rs. 1,80,469. The case is only concerned with the Rs. 3,459 which was remitted in the year of account out of unassessed profits of former years.

The Income-tax Appellate Tribunal held that this was not taxable because it represented income in respect of which there was an exemption by reason of the third proviso to Section 4 of the Act. The Commissioner asked the Tribunal to make the reference because he was of the opinion that the Tribunal had not appreciated the real effect of the proviso. At his request the Tribunal has referred the following question for the decision of this Court:—

"Whether in the circumstances of the case the sum of Rs. 3,459 was rightly assessed for the assessment year 1941-42."

Section 4 (1) (*b*) says that subject to the provisions of the Act, the total income of any previous year of a person includes all income, profits and gains from whatever source derived which if the person is resident in British India during the year (i) accrue or arise or are deemed to accrue or arise to him *in* British India during the year, or (ii) accrue or arise to him *without* British India during the year, or (iii) having accrued or arisen to him *without* British India before the beginning of the year and after the 1st April, 1933, are brought into or received in British India by him during the year. Therefore Section 4 (1) (*b*) deals with income which has arisen in British India, income which has arisen outside British India and income made in previous years which has been brought into British

India during the year of account. There are three provisos to Section 4, but we are only concerned with the third. It reads as follows :—

"Provided further that if in any year the amount of income accruing or arising without British India exceeds the amount brought into British India in that year, there shall not be included in the assessment of the income of that year so much of such excess as does not exceed four thousand five hundred rupees."

The draftsman might have expressed the intention of the Legislature in more simple terms, but what it means is this. If the amount of foreign income of the year of account exceeds the amount of foreign income brought into British India in that year, the assessee shall not pay tax on his foreign income *not brought into British India*, if such income does not exceed Rs. 4,500. If such income exceeds Rs. 4,500, the excess is taxable.

The case for the assessee is that if the amount remitted out of the untaxed profits of former years is less than Rs. 4,500, it is not subject to taxation at all because the concession given in the third proviso having applied must be deemed to continue to apply. The Income-tax Appellate Tribunal accepted this view, but with great respect we consider that it ignores the direct provisions of Section 4 (1) (*b*) (*iii*). That clause says in unambiguous language that if income which has accrued outside British India before the year of account is brought into British India in that year, it is subject to the tax. There is nothing in the third proviso which detracts from the effects of clause (*iii*). The proviso only says that in certain circumstances the assessee shall receive exemption from taxation in respect of foreign income up to and not exceeding Rs. 4,500 in a particular year, but it does not say that when the exempted income is brought into British India in a subsequent year, it shall not be taxable. The scheme of the Act is to tax all income made in British India and all income made abroad which is brought into British India, except, of course, income which is specifically exempted.

We hold that Section 4 (1) (*b*) (*iii*) is not controlled by the third proviso, which means that the Income-tax authorities rightly assessed the assessees in respect of the Rs. 3,459 brought into British India in the year of account.

As the question referred has been answered in favour of the Commissioner of Income-tax, the respondent must pay the costs Rs. 250.

Reference answered accordingly.

[IN THE BOMBAY HIGH COURT.]

MESSRS. GOVINDRAM BROS. LTD.

v.

COMMISSIONER OF INCOME-TAX, CENTRAL, BOMBAY.

SIR LEONARD STONE, C. J., and CHAGLA, J. August 27, 1946.

INDIAN INCOME-TAX ACT (XI OF 1922), SEC. 24 (2)—LOSS—CARRY FORWARD AND SET OFF OF LOSS—SEPARATE BUSINESS OR SAME BUSINESS—QUESTION OF FACT—LOSS IN SILVER SPECULATION—WHETHER CAN BE CARRIED FORWARD AND SET OFF AGAINST PROFIT FROM SPECULATION IN COTTON.

The test to be applied in order to determine whether two businesses are separate businesses or are the same business must be an inter-connection, an inter-lacing, an inter-dependence between, and a unity embracing, the two businesses.

The question whether a certain business is or is not the same business within the meaning of Section 24 (2) of the Income-tax Act is a question of fact.

From the date of its incorporation, the assessee company carried on speculation in various commodities in several markets. The speculation business was carried on in the same premises, by the same staff and with the aid of the same accounts. In the year 1939-40 the company carried on speculation in silver and incurred a loss. In the year 1940-41, the company carried on speculation in cotton and made a profit:

Held, *that on the facts of the case speculation in cotton was the same business as speculation in silver, and that the assessee company was entitled to set off the loss in speculation in silver carried forward from the assessment for 1940-41 against the profits from speculation in cotton considered in the assessment for 1941-42, under Section 24 (2) of the Income-tax Act, 1922.*

STONE, C. J.—*There can be no reason why a person, provided he conducts himself in a lawful manner, should not carry on the business of speculating in futures. The fact that in a particular year the assessee company as a speculator did not happen to speculate in a particular commodity or in a particular market did not make them carry on a separate or a new business when they recommenced to deal in that commodity or in that market.*

CHAGLA, J.—*Speculation by itself is not a nexus that connects the silver business with the cotton business. What would make those businesses into one business is not the factor of speculation or the fact that the assessee does not take delivery of those commodities but does forward business, but some other inter-connection or a nexus which has got to be found independently of the speculative character of those businesses.*

The way in which a case ought to be stated by the Appellate Tribunal pointed out.

Cases referred to :—

H. & G. Kinemas Ltd. *v.* Cook (H. M. Inspector of Taxes) [1933] (18 Tax Cas. 116).

Scales (H. M. Inspector of Taxes) *v.* George Thompson & Co., Ltd. [1927] (13 Tax Cas. 83).

Reference under Section 66 (1) of the Indian Income-tax Act (XI of 1922) by the Income-tax Appellate Tribunal: (Income-tax Reference No. 14 of 1944).

STATEMENT OF CASE.

"Under Section 66 (1) of the Indian Income-tax Act, 1922, we are submitting this reference to their Lordships of the High Court of Bombay, at the instance of the assessee whose application in this connection is marked Exhibit A. The Commissioner of Income-tax, Central, Bombay, has filed a written answer, Exhibit B.

2. The assessee is a private limited company trading under the style of Messrs. Govindram Bros. Ltd. The reference arises out of its assessment to income-tax for the charge year 1941-42 by the Income-tax Officer, Section VIII, Central, Bombay. The assessee took the assessment in successive appeals to the Appellate Assistant Commissioner and the Appellate Tribunal. Copies of the assessment and appellate orders are, respectively, Exhibits C, D and E.

3. The material facts which are substantially undisputed are narrated in paragraphs 1 and 2 of our judgment, Exhibit E. They may be briefly re-stated for the purpose of this reference. A part of the assessee's business is speculation in wheat, linseed, silver and cotton. Its year of account for the purpose of income-tax is the calendar year. In the year 1939, the assessee incurred a loss of Rs. 5,445 in speculation in linseed and wheat, and a similar loss of Rs. 1,33,875 in silver. In the assessment for 1940-41 in respect of the assessee's income of the previous year 1939, the total loss was adjusted to the assessee's income, profits and gains under one or more of the heads specified in Section 6 of the Act in accordance with the provisions of Section 24 (1). But it could not be wholly set off, and a net loss of Rs. 71,008 was carried to the next year.

4. In 1940, the assessee company speculated in New York cotton and made a profit of Rs. 2,04,827 which was considered in the assessment for 1941-42 in question. The assessee claimed to set off the loss of Rs. 71,008 carried forward as just stated, against its profits in the New York cotton, under Section 24 (2) of the Act. The Income-tax authorities did not permit the set off and we upheld their orders in the assessee's appeal No. 235-Bombay of 1942-43.

5. The only question before us was whether the loss which was attributable to speculation in silver could be set off in the following year against the income, profits and gains from speculation in cotton, having regard to the provisions of Section 24 (2) which provides that such a set off in a subsequent year can only be made against income, profits and gains from the "same

business." We held that speculation in silver, wheat and linseed and that in New York cotton were not the same businesses within the meaning of the section. Our finding raises a question of law which we shall formulate presently.

6. Before doing so, however, we think that it is necessary to briefly notice some of the averments made in the reference application. In paragraph 5, it is said that the Bench was under some misapprehension when it stated in the judgment that the assessee had conceded that the net loss that was carried forward was attributable to speculation in silver. It is denied that any such concession was made. We took that fact as conceded, inasmuch as it was not at all suggested that the net loss carried forward was attributable to any other business activity. In fact, the only two items of loss that were referred in the appeals were the loss in linseed and wheat and the loss in silver. We were not told that there was any loss from any other business activities of the assessee. The silver loss was over a lac of rupees and it was easy to infer that the net loss carried forward was attributable to speculation in silver alone, which fact was also obvious from the assessee's profit and loss account for the year 1939. Next, it is said in paragraph 3, clause (10), of the application that one of our findings of fact was that the profits that the assessee made in New York cotton in April-May, 1940, was the result of purchases made in October-November, 1939. We have recorded no such finding at all. Lastly, in paragraph 4, clause (6), it is said that the Bench failed to appreciate that in between the dates on which the applicant company entered into the New York contracts for purchases and final delivery the company had to pay and receive various sums of money on intermediate clearings according to the rules of the New York Cotton Exchange. But we are sure that no such fact was alleged or proved before us, not even a suggestion made in that connection.

7. The assessee has formulated not less than five questions as questions of law arising out of our judgment. The Commissioner on the other hand submits that only two questions of law arise. We think however that only one such question arises for reference to their Lordships and we formulate it as below :—

Question referred :—Whether in the circumstances of the case the assessee is entitled to set off the loss of Rs. 71,008 in silver speculation carried forward from the assessment for 1940-41 against the profits from speculation in New York cotton considered in the assessment for 1941-42, under Section 24 (2) of the Indian Income-tax Act, 1939 ?"

In accordance with the order of the High Court dated 12th October, 1944, the Income-tax Appellate Tribunal submitted the following supplementary statement of case.

SUPPLEMENTARY STATEMENT OF CASE.

" In this reference we submitted a statement of the case, together with a question of law, for their Lordships' opinion on January 30, 1944. But

their Lordships, by their order dated 12th October, 1944, have sent the reference back to record our findings more clearly, having regard to what they thought to be a conflict between the facts stated in paragraphs 3 and 5 of the statement of case.

2. We, however, respectfully submit that we are unable to state our finding more clearly than we have done. Their Lordships' direction appears to proceed from what they thought to be conflicting statement of facts in paragraphs 3 and 5 of the reference. But we respectfully desire to say that there is no such conflict, and we shall try to illustrate this view very briefly.

3. The assessee is a private limited company, and its objects as described in paragraph 3 of the Memorandum of Association are to carry on various kinds of businesses in any part of the world in any merchandise, goods, commodities etc. In the year of account, 1939, the assessees sustained a loss in speculation in linseed, wheat as well as silver. The whole of the loss could not be set off against the assessees' profits assessable for the year 1940-41, and, consequently, they carried forward a net loss of Rs. 71,008 which we held to be attributable to speculation in silver. In the account year 1940, they made a large profit in speculation in New York cotton and claimed to set it off against the loss carried forward. We held that the set off was not allowable under Section 24 (2) of the Indian Income-tax Act, the speculation business in silver and the speculation business in cotton being, in our opinion, different businesses. Our findings were that the assessees did not do any business in cotton in 1939, and that the loss in question was loss in silver.

4. Their Lordships appear to have laid stress upon our statement of fact in paragraph 3 of the reference. The fact stated there is:—"A part of the assessees' business is speculation in wheat, linseed, silver and cotton." Their Lordships contrast this statement with several others which they have pointed out from our judgment.

5. While stating that a part of the assessees' business is speculation in wheat, linseed, silver and cotton, we were only giving a description of some out of the manifold business activities of the assessees described in clause 3 of their Memorandum of Association. We mentioned these activities in particular because they were relevant. The statement in question was not intended to describe the activities with reference to any particular year of account. In this connection, we solicit their Lordships' attention to the remaining portion of paragraph 3 as well as paragraph 4 of the case. In these paragraphs we described the businesses that the assessee company carried on in the particular years of account. We have recorded a clear finding that in account year, 1939, the assessees' business relevant to the question was in wheat, linseed and silver only while that in 1940 was in cotton.

6. Read in this light we submit that any conflict between the opening statement of paragraph 3 and the rest of the statements would disappear. On this point we would respectfully refer their Lordships to an affidavit filed after remand by Mr. Pralhadrai who is one of the directors of the assessee company. In paragraph 1 it is stated:—"It may be that in any particular accounting year the applicants may not have speculated in any particular market or in any particular commodity but that was because the applicants thought it not advisable or expedient to do so during the particular accounting year." This statement amounts to a substantial admission that the speculation business done in 1939 and that in 1940 was in different commodities.

7. Then on the point as to whether there was any speculation business in cotton in the year 1939, all that was proved before us was the purchase of 12,500 bales of cotton, in October and November 1939, for April, 1940 settlement, and we held that the purchase alone did not amount to business. Their Lordships have observed that the purchase was one limb of the business, the other limb being the sale in April, 1940. But we were considering the question of set off of profits against losses, and, in our humble opinion, profits do not come into being by the limb or operation of purchase alone. Before profits can arise there must be a sale. And on this point we respectfully cite *Commissioner of Income-tax, Bombay* v. *Chunilal B. Mehta* [1], in which Sir George Rankin delivering the judgment of the Privy Council observed:—

"Here the profit is a difference between sale and purchase both effected in New York and their set off . . . . . ." (page 527 of the report).

In the present case we were not concerned with whether the purchase amounted to an operation or limb of the business, but with the arising of the profit in any particular year. We held that the profit in cotton pertained to account year 1940, and that there being no business in cotton in 1939 the loss in silver cannot be set off against the profits in cotton.

8. The affidavit that we have referred to is annexed to this supplementary statement, Exhibit F.* It is stated therein that speculation business in different markets and in different commodities constitutes one and the same business. That is a matter of argument. Further, it is stated that speculation business is one unified and organised activity of the assessees and that it is carried on with the same staff and with the aid of the same accounts and in the same premises. This fact was not before us when we heard and disposed of the assessees' appeal. And we are unable to include it in the case at this stage of the proceedings and equally because it requires to be established by evidence which is not before us."

(1) [1938] 6 I.T.R. 521.

* The relevant paragraph of this affidavit is quoted in the judgment of Stone, C.J.

Sir Jamshedji Kanga with *R. J. Kolah*, for the assessee.
Motilal Setalvad, for the Commissioner.

JUDGMENT.

STONE, C. J.—This is a reference under Section 66 (1) of the Income-tax Act, and the question which we are asked, in our advisory capacity, to express an opinion upon, is whether the loss which was incurred by the assessee company and which was attributable to speculation in silver can be set off, in the following year, against the income, profits and gains in speculation in cotton, having regard to the provisions of sub-section 24 (2) of the Income-tax Act. That sub-section provides that such a set off in a subsequent year can only be made against income, profits and gains from "the same business."

The question as framed by the Tribunal in the original case was :—

"Whether in the circumstances of the case the assessee is entitled to set off the loss of Rs. 71,008 in silver speculation carried forward from the assessment for 1940-41 against the profits from speculation in New York cotton considered in the assessment for 1941-42, under Section 24 (2) of the Indian Income-tax Act, 1939 ? "

Sub-section 24 (2) is in these terms :—

"Where any assessee sustains a loss of profits or gains in any year, being a previous year not earlier than the previous year for the assessment for the year ending on the 31st day of March, 1940, under the head 'Profits and gains of business, profession or vocation', and the loss cannot be wholly set off under sub-section (1), the portion not so set off shall be carried forward to the following year and set off against the profits and gains, if any, of the assessee from the same business, profession or vocation for that year."

There follows a provision for a still further carry forward. The material words, which are to be noted, are that it must be from "the same business, profession or vocation."

In their judgment the Appellate Tribunal commenced in paragraphs 1 and 2 by stating the facts which are as follows :—

"1. This appeal relates to an assessment made upon the appellant company for the charge year 1941-42. It is a private limited company and was registered on 16th November, 1937. Its various objects are described in paragraph 3 of the Memorandum of Association which include carrying on business as managing agents of the Seksaria Cotton Mills Ltd., any trade, business, manufacture or commercial operations in any part of the world in any merchandise, commodities, goods, etc., and establishing and maintaining agencies at any place or places in the world for the conduct of the business of the company. The 'previous year', *i.e.*, account year, of the company for the purpose of income-tax is the calendar year (1940).

2. A part of the assessee company's business is speculation in wheat, linseed, silver and cotton. In the account year 1939 it incurred a loss of Rs. 5,445 in linseed and wheat, and Rs. 1,33,875 in silver. In the assessment of 1940-41 the loss was adjusted against income, profits and gains of the company from other sources. But it could not be wholly set off, and a net loss of Rs. 71,008 was carried to the next year. In the account year 1940 the assessee speculated in the New York cotton and made a profit of Rs. 2,04,827 which was brought into the present assessment for 1941-42. It claimed to set off the net loss of Rs. 71,008 carried forward as just stated, against the profit in New York cotton. The Income-tax Officer held that the set off could not be allowed having regard to Section 24 (2) of the Indian Income-tax (Amendment) Act, 1939. His view was upheld by the Appellate Assistant Commissioner."

The Tribunal held that the speculations in New York cotton were not the same business as speculation in silver in Bombay.

In that state of the record this matter came before us in October, 1944, and in referring the case back to the Tribunal my learned brother Kania delivering the judgment of this Court on the 12th October, 1944, said :—

"The question whether the business is the same, under Section 24 (2) is a question of fact. It is a conclusion to be drawn from various facts which are established from the records produced before the Tribunal. The question, which this Court can consider is whether any evidence exists for the conclusion of the Tribunal. Apart from that, the Tribunal being the final fact-finding authority, this Court cannot go into the question. From that aspect the two statements found in the statement of the case appear to be conflicting. In paragraph 3 it has stated : 'A part of the assessee's business is speculation in *wheat, linseed, silver* and cotton.' Towards the end of paragraph 5 it has stated : 'We held that speculation in *silver, wheat* and *linseed* and that in New York cotton were not the same business within the meaning of the section.' It may be noted that at this stage also the Tribunal has omitted to notice the word 'cotton' in describing the nature of the business of the assessee, as it had first described."

The supplemental case returned to us by the Tribunal, and which is now before us is highly unsatisfactory. The Tribunal appear to be far more concerned with excusing the statements of fact in the first case, which are unquestionably contradictory, than with complying with the directions of this Court given under Section 66 (4) of the Income-tax Act. In the supplemental case the Tribunal states : "We have recorded a clear finding that in account year, 1939, the assessees' business relevant to the question was in wheat, linseed and silver only, while that in 1940 was in cotton." And finally they stated :—

"The affidavit that we have referred to (*i.e.*, an affidavit of Mr. Pralhadrai Brijlal) is annexed to this supplementary statement, Exhibit-F. It is stated therein that speculation business in different markets and in different commodities constitutes one and the same business. That is a matter of argument. Further, it is stated that speculation business is one unified and organised activity of the assessees and that it is carried on with the same staff and with the aid of the same accounts and in the same premises. This fact was not before us when we heard and disposed of the assessees' appeal. And we are unable to include it in the case at this stage of the proceedings and equally because it requires to be established by evidence which is not before us."

The matter was referred back to the Tribunal to record its finding of fact more clearly, and implicit in that direction is the taking of further evidence, if there is no other way of determining facts in order that the Tribunal may make its finding clear. For the Tribunal to say that because a fact was not before it when they disposed of the assessee's appeal, "we are unable to include it in the case at this stage of the proceedings," is a most surprising statement and is one which indicates that the Tribunal does not appreciate the duties cast upon it when this Court refers a matter back under Section 66 (4). The reference back to the Tribunal was to record its finding more clearly and after a lapse of one year and ten months—the matter now comes back with nothing new except the affidavit of Mr. Pralhadrai Brijlal, which is annexed to the supplemental case. The delay is not due to any fault of the Tribunal, but it is very oppressive on the assessee, who under the proviso to Section 30 of the Act has had to pay the full amount of the claim.

To the affidavit of Mr. Pralhadrai Brijlal there has been no affidavit in answer, and no application to cross-examine the deponent upon his affidavit has been made. Mr. Setalvad on behalf of the Commissioner states, and I think, very fairly and properly, in the circumstances, that he is prepared to accept the affidavit as it is uncontroverted.

Paragraph 1 of the affidavit which is the only paragraph relevant to what we have to consider says :—

"From the date of its incorporation a part of the business of the applicants consisted of speculation in different markets in different commodities. It may be that in any particular accounting year the applicants may not have speculated in any particular market or in any particular commodity but that was because the applicants thought it not advisable or expedient to do so during the particular accounting year. From the commencement speculation business in different markets and in different commodities constituted one and the same business of the applicants. In proof of the fact that the applicants' dealings in several markets in different commodities

form part of the same business I produce the following evidence. One of the objects of the incorporation is to carry on speculation business in any part of the world in any commodity. For brevity's sake I crave leave to refer to the memorandum and articles of the company when produced. Speculation business is one unified and organised activity of the applicants. Speculation business is carried on with the same staff and with the aid of the same accounts and in the same premises. The nature of all speculative business is the same and the difference in commodities or the difference in the markets makes no difference to the nature of the speculative business."

Mr. Setalvad has referred us to the case of *Scales* (*H. M. Inspector of Taxes*) v. *George Thompson & Co., Limited*[1]. In that case the question arose whether the company was carrying on one business or two businesses, the activities of the company being underwriting and shipping, and Rowlatt, J., said at page 89 :—

"That method of book-keeping does not seem to me to throw any light upon this matter at all. I think the real question is, was there any interconnection, any inter-lacing, any inter-dependence, any unity at all embracing those two businesses; and I should have thought, if it was a question for me, that there was none. But I do not think it was a question of law. I think the Commissioners had ample evidence upon which they could decide, and they did so decide."

As has been pointed out by Mr. Justice Finlay in the case of *H. & G. Kinemas, Ltd.* v. *Cook*[2], which is a very well-known case, to which this Court is not infrequently referred, the only matter which this Court in its advisory capacity can consider on a finding of fact is whether there is any evidence upon which the Tribunal could come to the conclusion to which it in fact came. To quote from the language of Mr. Justice Finlay (page 121):

"I have come to the conclusion in this case that I cannot interfere with the decision of the Commissioners. I desire to say quite definitely that it is their decision and not mine. It is not necessary that I should express an opinion, and I do not express an opinion, as to whether, if I had been in their position, I should have arrived at the same conclusion. There are two reasons, one of general application and one of special application, for saying this. The one of general application is that this is, in my opinion, a pure question of fact. It accordingly results that all questions of fact and of degree are for the Commissioners, and it is never proper for this Court to interfere, unless it is prepared to say that there was no evidence upon which the finding could be made."

The Tribunal would do well to study the case submitted to the Court which is fully set out in this report, and to treat it as a guide to the way in which a case ought to be stated by them. In view of the delays which

(1) (1927) 13 Tax Cas. 83. (2) (1933) 18 Tax Cas. 116, at p. 121.

have taken place, we are very reluctant to send this matter back once again to the Tribunal to comply with our directions given on the 12th October, 1944, and in view of Mr. Setalvad's statement on behalf of the Commissioner, that he accepts the affidavit of Mr. Brijlal as being uncontroverted, we are prepared to proceed with the matter.

Mr. Setalvad has submitted that there is no such thing as the business of a speculator and that the position must be regarded as if the assessee company is carrying on separate businesses as dealers on the New York Cotton Exchange and as dealers on the Bombay Bullion Exchange. But there is no evidence of this. On the other hand, I can see no reason why a person, provided he conducts himself in a lawful manner, should not carry on the business of speculating in futures. One of the dictionary meanings of "speculation" is "an act or instance of speculating: a commercial venture or undertaking of an enterprising nature especially, one involving considerable financial risk on the chance of unusual profit", (see Oxford Dictionary, New Series, Vol. IX, page 559).

The fact that in a particular year the assessee company as a speculator does not happen to speculate in a particular commodity or in a particular market does not in my opinion make him carry on a separate or a new business when he recommences to deal in that commodity or in that market. I cannot see how a business which speculates in any commodity in which it anticipates that it will make a profit, is, for the purpose of determining whether it is carrying on one business or a multiplicity of businesses, in any different position from a stock-broker, or a book-maker or a man who keeps a general store. Having carefully considered the original case, the supplemental case and the affidavit annexed to it, there is not, in my opinion, any evidence that the assessee company is carrying on more than one business, upon which any such finding could be based. There is no clear finding by the Tribunal at all, and in such circumstances the case must be decided by the Court on the materials before it. The evidence contained in the affidavit of Mr. Brijlal is all in favour of there being only one business, and that evidence must, in my opinion, be accepted. Accordingly, the question referred to us must be answered in the affirmative. The Commissioner must pay the costs.

CHAGLA, J.—It is with considerable hesitation that I have come to the same conclusion as the learned Chief Justice. The jurisdiction that we are exercising under the Income-tax Act is a purely advisory jurisdiction. The Appellate Tribunal is the final fact finding authority, and in our advisory capacity it is not open to us to go behind the findings of facts arrived at by the Tribunal. It is only if we come to the conclusion that there was no evidence to justify a particular finding of fact that it is open to us to set aside the particular finding arrived at by the Tribunal. Therefore the

Statute has cast upon the Tribunal very important duties and responsibilities and I regret to say that the Tribunal does not always appreciate or realise its own duties and responsibilities. If we have to exercise our advisory jurisdiction in the manner in which the Statute expects us to do, it is essential that the Tribunal must find facts clearly and explicitly. It is only on such clear and explicit findings of facts that we can satisfactorily exercise advisory jurisdiction.

Now there can be no question that whether a certain business is or is not the same business within the meaning of Section 24, sub-section (2), of the Act is a question of fact, and it is for the Tribunal to find that fact. Unfortunately in this case the Tribunal has deliberately ignored important pieces of evidence that were placed before it in the form of the affidavit to which the learned Chief Justice has referred. Although in the judgment of Mr. Justice Kania the Tribunal was given liberty to call further evidence to arrive at its finding of fact, it refused to take the materials contained in the affidavit into consideration. The question is whether apart from those materials contained in the affidavit there is any other evidence on the record which would justify the finding of fact arrived at by the Tribunal. Now Mr. Justice Rowlatt in the case to which the learned Chief Justice has just referred (*Scales* v. *George Thompson & Co., Ltd.*[1]) has laid down the test which should be applied in order to determine whether two businesses are separate businesses or are the same business. There must be, as the learned Judge observes, an inter-connection, an inter-lacing and an inter-dependence between the two businesses and there must be a unity embracing the two businesses. Now, with great respect to the learned Chief Justice, I do not agree that "speculation" by itself is a nexus that connects the silver business of the assessee with the New York cotton business. I do not frankly understand the expression that a man is doing business in speculation. "Speculation" in its legal connotation does and can only mean that a man is doing forward business. The question will still remain: in what commodity is he doing forward business? He may be doing forward business in silver; he may be doing forward business in cotton; or he may be doing forward business in linseed. But what would make those businesses into one business is not the factor of speculation or the fact that he does not take delivery of those commodities but does forward business, but some other inter-connection or a nexus which has got to be found independently of the speculative character of those businesses. Therefore the main question to which the Tribunal should have applied its mind was in my opinion whether there was any inter-connection between the silver business of the assessee and the New York cotton business of the assessee, and I have looked through the record

(1) (1927) 13 Tax Cas, 83,

in vain to find whether the Tribunal ever approached the question from that aspect. Unfortunately the view that the Tribunal took was that the question whether the business is the same business within the meaning of Section 24, sub-section (2), of the Act was a question of law and not a question of fact and, therefore, the whole of the statement of facts is vitiated by this erroneous consideration. If the Tribunal had correctly approached the question and had considered this particular matter as a question of fact, then it would have given the necessary findings which we might have considered; but having looked upon it as a question of law, the Tribunal's statement of the case and judgment contain arguments and discussion of law rather than findings of fact or reference to evidence on which its conclusions are based.

Therefore, the course open to us would have been to have sent the matter back to the Tribunal for determining the necessary questions of fact; but the matter has already been referred to the Tribunal once, and I do not think it is fair to the assessee that the matter should be referred back again. On the whole I am satisfied and I come to the same conclusion as the learned Chief Justice that as the record stands, there is no evidence on which the findings of facts of the Tribunal can be justified, namely, the business of cotton and the business of silver is not the same business within the meaning of Section 24, sub-section (2), of the Act.

I, therefore, agree that the question referred to us should be answered in the manner suggested by the learned Chief Justice.

Reference answered accordingly.

[IN THE PATNA HIGH COURT.]

THE PROVINCE OF BIHAR

v.

MAHARAJA MAHADEVASHRAM PRATAP SAHI.

FAZL ALI, C. J., MANOHAR LALL and SINHA, JJ.

January 9, 1946.

BIHAR AGRICULTURAL INCOME-TAX ACT (VII OF 1938), SEC. 25 (1)—REFERENCE BY BOARD OF AGRICULTURAL INCOME-TAX *Suo Motu* AFTER TERMINATION OF PROCEEDINGS—COMPETENCY—SCOPE OF SEC. 25 (1).

The assessee was assessed to agricultural income-tax for the assessment years 1938-39 and 1939-40 on the 31st August, 1939, and the 19th March, 1940, respectively, on certain sums which included interest on arrears of rent. No appeal was preferred against these orders, but on 22nd September, 1941, he filed an application under Section 27, Bihar Agricultural Income-tax Act, before the Agricultural Income-tax Officer stating that it was not clear whether interest on arrears of rent was agricultural income, that it had been assessed by both the Agricultural Income-tax Department and the Indian

Income-tax Department and that the mistake, which was apparent from the record, should be rectified. The officer declined to give him any relief on the 7th November, 1941. An appeal was preferred to the Commissioner and he allowed it on 27th October, 1942, on the ground that interest on arrears of rent was not agricultural income according to the decision of the Patna High Court in RAM RAN VIJAY PRASAD SINGH *v.* PROVINCE OF BIHAR[1]. *Sometime later the Commissioner moved the Board to revise the order passed on 27th October, 1942, but on 17th June, 1943, the Board took the view that although the order of the Commissioner was illegal, the Board had no power to review it. Under Section 25 (1) of the Act, the Board on its own motion referred to the High Court the question whether the order of the Commissioner dated 27th October, 1942, was illegal:*

Held, *that the reference under Section 25 (1) was incompetent inasmuch as the assessment proceedings against the assessee had already terminated and there was no pending proceeding under the Act in the course of which the question of law referred to the High Court could arise;*

Held further, *that even assuming that a series of incompetent proceedings could be called proceedings under the Act, the proceedings had terminated and the Board had no power to move under Section 25 (1).*

The scheme of the Act indicates clearly that after an assessment has been made or after any proceeding under the Act has terminated, the assessee alone has been given the right under the Act to ask for a reference to the Court under Section 25 (2) in cases where an assessment has been made or a revisional order enhancing the assessment has been passed or it is otherwise prejudicial to the assessee or if a decision by a Board of Referees has been made.

Cases referred to :—

Commissioner of Income-tax, Madras *v.* Zemindar of Kirlampudi [1932] (I.L.R. 55 Mad. 830; A.I.R. 1932 Mad. 436; 138 I.C. 289.)

Ram Ran Vijay Prasad Singh *v.* Province of Bihar [1942] (10 I.T.R. 446).

Reference under Section 25 (1) of the Bihar Agricultural Income-tax Act (VII of 1938) by the Board of Agricultural Income-tax, Bihar: (Miscellaneous Judicial Case No. 72 of 1943).

STATEMENT OF CASE.

"Case stated under Section 25 (1) of the Bihar Agricultural Income-tax Act, 1938 (Act VII of 1938), by the Bihar Board of Agricultural Income-tax on its own motion referring a question of law whether a Commissioner of Agricultural Income-tax has power to revise an order passed under Section 27 of the Act and to vary an assessment against which no appeal had been filed under Section 22 of the Act. The facts are as follows :—

1. On 31st August, 1939, the Hathwa Estate (now under the Court of Wards) (hereinafter referred to as the assessee) was assessed to agricultural income-tax on its agricultural income for 1345 fasli. The income assessed

(1) [1942] 10 I.T.R. 446.

included a sum of Rs. 24,475 being interest on arrears of rent. A copy of the assessment order is enclosed (ExhibitA).

2. On 19th March, 1940, the assessee was again assessed to agricultural income-tax on its agricultural income for 1346 fasli. The income assessed included a sum of Rs. 18,441 being interest on arrears of rent. A copy of the assessment order is enclosed (Exhibit B).

3. No appeal under Section 22 of the Act was filed by the assessee against either of these assessments.

4. In a petition, dated the 22nd September, 1941, the assessee applied to the Agricultural Income-tax Officer, Muzaffarpur Circle, under Section 27 of the Act to rectify, what he called, the mistake of including interest on arrears of rent in the assessment and applied for a refund of the tax assessed on the two amounts mentioned. The Agricultural Income-tax Officer, Muzaffarpur Circle, rejected the petition on 7th November, 1941, on the ground that the petition was time-barred and that the ruling of the Calcutta High Court, dated the 3rd July, 1940, (in the case of *Commissioner of Income-tax* v. *Manager, Radhika Mohan Roy Wards Estate*[1]), on the basis of which the assessee was claiming refunds, did not apply as the assessments for the years 1938-39 and 1939-40 were made long before. A copy of the petition and of the Agricultural Income-tax Officer's order are enclosed (Exhibits C and D).

5. Again in a revision petition filed on the 3rd December, 1941, the assessee moved the Commissioner of Agricultural Income-tax, Tirhut Division, to revise the order of the Agricultural Income-tax Officer refusing the refund. A copy of the revision petition is enclosed (Exhibit E).

6. On 27th October, 1942, the Commissioner of Agricultural Income-tax passed an order 'allowing the appeal' and directed the exclusion of the sums of Rs. 24,465 and Rs. 18,441 from the assessments of 1345 and 1346 fasli respectively. A copy of his order is enclosed (Exhibit F).

In the opinion of the Board of Agricultural Income-tax, as set forth below, the Commissioner's order was illegal and *ultra vires* :—

(*a*) No revision lay to the Commissioner against the order refusing the grant of a refund. Section 24 of the Act provides for revision of an appellate order and in the cases there was no appeal and there is no other provision for revisional power except under Section 24. The application for revision ought not to have been admitted at all.

(*b*) The Commissioner states in his order "the appeal is allowed." In fact there was no appeal. Even if the revisional petition is treated as an appeal it was long time-barred under Section 22 (2) of the Act read with rule 13 of the Bihar Agricultural Income-tax Rules, 1939. The order revising the assessment was in the circumstances *ultra vires* of the Commissioner.

(1) [1940] 8 I.T.R. 460.

(c) On merits the order of the Agricultural Income-tax Officer refusing a refund was correct. Section 27 of the Act provides for rectification of a mistake apparent from the record. The alleged mistake only came to the notice of the assessee when the Calcutta High Court ruled that interest on arrears of rent is not agricultural income. The petition for refund was in effect a time barred appeal presented to a wrong authority asking for retrospective effect to be given to the ruling of the High Court of another province. A copy of the Board's resolution is enclosed (Exhibit G)."

Advocate-General, for the Province of Bihar.

Baldeva Sahay and *B. B. Saran*, for the assessee.

JUDGMENT.

MANOHAR LALL, J.—This reference by the Board of Agricultural Income-tax, Bihar—hereinafter called the Board—under Section 25 (1) of the Bihar Agricultural Income-tax Act, 1938—hereinafter referred to as the Act—is made in peculiar circumstances to ask the opinion of the Court whether the order of the Commissioner of Agricultural Income-tax dated the 27th October, 1942, was illegal.

The assessee, Maharaja Bahadur of Hathwa, was assessed on the 31st August, 1939, by the Agricultural Income-tax Officer for the assessment year 1938-39 on a certain sum which included Rs. 24,475 as representing interest on arrears of rent in the year 1345 fasli being the previous year for that assessment. For the following year 1939-40 the assessee was assessed by the Agricultural Income-tax Officer on the 19th March, 1940, for a certain sum including Rs. 18,441 as representing interest on arrears of rent in the year 1346 fasli. No appeal was preferred against these two orders. An application under Section 27 of the Act was filed by the assessee on the 22nd September, 1941, before the Agricultural Income-tax Officer inviting his attention to the fact that the same amounts of interest on arrears of rent in the years 1345 and 1346 fasli have been assessed both by the Agricultural Income-tax Department and by the Indian Income-tax Department. Attention was also drawn to the fact that in the years in question it was not definitely certain whether the questioned amount was taxable under the Agricultural Income-tax Act or under the Indian Income-tax Act. The assessee accordingly prayed that on principles of equity and justice and even under the provision of Section 27 of the Act, the mistake, which was apparent on the face of it, should be rectified. It was urged that the delay in making the application should be condoned, as the matter was not free from doubt and has been cleared only recently by a decision of the Calcutta High Court. By an order dated the 7th of November, 1941, the Agricultural Income-tax Officer declined to give any relief to the assessee as in his view the Madras High Court ruling, *Zemindar of Kirlampudi*[1], was applicable to the case and further, " As assessments for 1938-39 and

(1) (1932) I.L.R. 55 Mad. 830.

1939-40 were made prior to 3rd July, 1940, Calcutta High Court ruling also did not apply. This matter is still *sub-judice* and the point has been referred to Patna High Court for decision in the case of *Maharajadhiraj of Darbhanga*. Hence the petition filed cannot come under Section 27."

Against this order an appeal was preferred to the Commissioner of Agricultural Income-tax who on the 27th October, 1942, passed this order :—

"It has been held in the Full Bench ruling of the Patna High Court in Miscellaneous Judicial Case No. 99 of 1940*, on 1st April, 1942, that interest on such rents is not part of the rent, and therefore it does not come within the definition of agricultural income for the purpose of the Bihar Agricultural Income-tax Act, 1938.

The appellant is therefore entitled to the exclusion of Rs. 24,475 from his income in the year 1345 fasli and Rs. 18,441 in 1346 fasli.

The appeal is allowed."

It will be noticed that the application under Section 27 of the Act was filed before the Agricultural Income-tax Officer beyond the period prescribed under Section 27 (1) and further that no appeal lay to the Commissioner against an order refusing to grant to the assessee any relief under Section 27. Sometime later—the exact date does not appear from the record—the Commissioner of Agricultural Income-tax moved the Board to revise the order under Section 24 of the Act passed on the 27th October, 1942—the letter or the application by the Commissioner to the Board has not also been produced before us.

The Board on the 17th of June, 1943, took the view that although the Commissioner's order was illegal, the Board had no power to review it. It further held that Section 27 of the Act had no application and, therefore, the Agricultural Income-tax Officer was right in rejecting the prayer of the assessee. It also pointed out: "No revision lay as Section 24 only provides for revision of an order passed on appeal under Section 22 and, as already stated, there was no appeal. The Commissioner made a further mistake by adding the words 'the appeal is allowed.' There was no appeal before him. Even if it had been an appeal it was long time-barred under Section 22 (2) read with rule 13, but the Commissioner purported to act under Section 24 and under sub-section (3) of that section any order passed in revision is final subject to a reference to the High Court under Section 25."

It will be observed that the reference to this Court has been made by the Board not at the instance of the assessee but on its own motion. Under Section 25 (1) "if, in the course of any assessment under this Act or any proceeding in connection therewith other than a proceeding under Chapter VI (the proceeding under Chapter VI relates to offences and penalties), a question of law arises, the Board may, either of its own motion or on reference

* Since reported as *Ram Ran Vijay Prasad Singh* v. *The Province of Bihar* [1942] 10 I.T.R. 446.

from any Agricultural Income-tax authority subordinate to it, draw up a statement of the case and refer it with its own opinion thereon to the High Court." In the present case the assessment proceedings against the assessee had already terminated and there was no pending proceeding under the Act in the course of which the question of law referred to us could arise. The scheme of the Act indicates clearly that after an assessment has been made or after any proceeding under the Act has terminated, the assessee alone has been given the right under the Act to ask for a reference to the Court under Section 25 (2) in cases where an assessment has been made or a revisional order enhancing the assessment has been passed or it is otherwise prejudicial to the assessee or if a decision by a Board of Referees has been made. In these circumstances the assessee and the assessee alone has been given a right under the Act to ask for a reference to the High Court. The assessee can move the Board in other cases under Section 25 (1) and in those circumstances the Board may at its discretion make a reference to the High Court or again in the course of any assessment or in the course of any proceeding under this Act, any Agricultural Income-tax authority subordinate to the Board may make a reference to the Board for stating the question to the High Court.

The learned Advocate-General argued that there was a proceeding here which was started on the application of the assessee under Section 27 and when the Commissioner purported to exercise an appellate power there was a proceeding before him and even if he had no appellate power but purported to exercise a revisional power, there was still a proceeding before him, and, therefore, the requirements of Section 25 (1) have been satisfied. Even assuming that a series of incompetent proceedings could be called proceedings under the Act, the proceedings had terminated and the Board had no power to move under Section 25 (1).

It was argued by the learned Advocate-General that if the Commissioner or the Collector or the Income-tax Officer under the Act makes a mistake in favour of the assessee on a question of law the result would be that there will be no remedy to correct such a mistake. The short answer to this argument is that no such remedy is provided in the Act to the Agricultural Income-tax authorities unless a reference is made to the High Court in the course of a proceeding which may be pending either before the first officer or before the appellate or revisional officers.

In my opinion the reference is incompetent, and I would decline to answer the question referred to us.

In the circumstances each party will bear his own costs in this Court.

FAZL ALI, C. J.—I agree.

SINHA, J.—I agree.

Reference not answered.

[IN THE BOMBAY HIGH COURT.]

D. R. SHAHAPURE

v.

COMMISSIONER OF INCOME TAX, BOMBAY.

SIR LEONARD STONE, C. J., and KANIA, J. September 11, 1944.

INDIAN INCOME-TAX ACT (XI OF 1922), SEC. 16 (1) (c), THIRD PROVISO—SETTLEMENT OF INCOME WITHOUT TRANSFER OF ASSETS—ENTRY IN ACCOUNT BOOKS TO INVEST CERTAIN SUM IN BUSINESS FOR WIFE'S USE—IRREVOCABLE COVENANT TO PAY FIXED SUM TO HER ANNUALLY FOR HER LIFE—SUM DERIVED FROM INVESTMENT—WHETHER ASSESSABLE AS HUSBAND'S INCOME—DUTY TO MAINTAIN WIFE—EFFECT OF—SCOPE OF SEC. 16 (1) (c), THIRD PROVISO.

The third proviso to Section 16 (1) (c) of the Indian Income-tax Act, 1922, applies even to cases where there has been no transfer of assets but only a settlement of income from assets remaining the property of the disponer.

The assessee, with a view to make a provision for his fifth wife, made an entry in his business books which, after reciting that at the time of her marriage he had promised that out of his estate he would hand over to her an estate worth Rs. 20,000 for her benefit up to her death, stated as follows: "The capital supplied to you will remain entirely mine but you will get the income over it up to the end of your life. This capital I will not take back up to the end of your life but I will do business for you on this capital and see that you get Rs. 600 per annum for you . . . . . . you can spend Rs. 600 as you like and if there is any extra income you can utilise it for anything you wish to buy . . . . After your death the said capital will be mine . . . . ." No specific assets were set aside to meet this sum of Rs. 20,000 and there were no further entries in the books with regard to it. In the relevant accounting period a sum of Rs. 280 was derived by investment:

Held, *that the entry was an irrevocable covenant to pay the income accruing on Rs. 20,000 with a guarantee that there should be Rs. 600 a year, and inasmuch as "settlement" is defined in Section 16 (1) (c) of the Indian Income-tax Act as including "a covenant, agreement or arrangement" the case was covered by the third proviso to Section 16 (1) (c) and the income which was paid to the wife under this covenant could not be deemed to be the income of the assessee under the first part of Section 16 (1) (c).*

Where a husband makes a settlement for the exclusive and independent maintenance of his wife it cannot be said that he receives an indirect benefit from it within the meaning of the third proviso to Section 16 (1) (c) merely because he is under a legal obligation to maintain his wife.

RAMJI KESHAVJI v. COMMISSIONER OF INCOME-TAX, BOMBAY [1945] (13 I.T.R. 105) *referred to.*

Reference under Section 66 (1) of the Indian Income-tax Act (XI of 1922) by the Income-tax Appellate Tribunal: (Income-tax Reference No. 22 of 1943).

STATEMENT OF CASE.

"This is an application by the assessee under Section 66 (1) of the Indian Income-tax Act, seeking to refer to the High Court a question of law arising out of the order of the Tribunal in R.A.A. No. 127-(Bombay) of 1942-43.

2. The facts of the case are simple. The assessee made an entry on May 6, 1937, in his account book embodying the family arrangement whereby he set apart a sum of Rs. 20,000 stipulating *inter alia* that under certain conditions the income arising from the investment of the said sum belonged to his wife, Bai Shantibai, who was, however, to have no right to or interest in the capital itself. During the relevant accounting period, by investment of the said sum in the money-lending business of the assessee, an income of Rs. 280 was derived. The Income-tax Officer included it in the taxable income of the assessee and in appeal the Appellate Assistant Commissioner affirmed the same in the view that since the income arose from the assets transferred by the assessee directly to his wife otherwise than for adequate consideration, it fell to be assessed in the hands of the assessee under Section 16 (3) (*a*) (*iii*) of the Act.

3. The assessee appealed against this order to the Tribunal. The Tribunal found on a construction of the aforementioned account entry, that the capital itself had not been transferred and that consequently there was no transfer of the assets to attract the application of Section 16 (3) (*a*) (*iii*). The inclusion of the income of Rs. 280 in the assessable income of the assessee was, however, upheld by the Tribunal on the ground that according to the arrangement the assets themselves remained the property of the settlor and that for that reason the income in question should be deemed to be the income of the assessee-settlor under the first part of Section 16 (1) (*c*). The assessee's contention that in such an event the third proviso would apply to the case was rejected by the Tribunal.

4. We are of the opinion that out of this finding the following question of law arises and we refer the same to the High Court of Judicature at Bombay :—

'Whether the sum of Rs. 280 is income arising from assets remaining the property of the assessee, and as such whether it has to be deemed, under the first part of clause (1) (*c*) of Section 16 of the Income-tax Act, to be the income of the assessee?'"

D. D. Yennemadai, for the assessee.

M. C. Setalvad, for the Commissioner.

JUDGMENT.

STONE, C. J.—This is a reference under Section 66 (1) of the Indian Income-tax Act. The question submitted to the Court is in these terms:—

"Whether the sum of Rs. 280 is income arising from assets remaining the property of the assessee, and as such whether it has to be deemed, under the first part of clause (1) (c) of Section 16 of the Income-tax Act, to be the income of the assessee?"

The income in question arises by virtue of an entry which the assessee made in his business books on 6th May, 1937. The relevant parts of that entry are as follows:

"To-day I am making a family arrangement for my own good. All my estate belongs to me and is acquired by me and hence no one has a claim on this estate except me. I have got full right to dispose of this estate or make some arrangement about it as I like."

The assessee then states that his first four wives are dead and that he is to marry again. He states that his age is 61 years. He then continues that at the time he made arrangements with the fifth wife's parents, "I promised that out of my estate I will hand over to you an estate worth Rs. 20,000 for your benefit only up to your death." Then after stating some provision about the brother of his wife, and the marriage expenses, the entry continues as follows:—

"Out of the amount of Rs. 20,000 referred to above you have to give to your brother and for your marriage expenses. The capital supplied to you will remain entirely mine but you will get the income over it up to the end of your life. This capital I will not take back up to the end of your life but I will do business for you on this capital and see that you will get Rs. 600 per annum for you. I will pay for any loss in this business. If I become incapable of doing this business, you are free to employ somebody to do business for your sake. But such a man must give a guarantee that he will give me back the amount after your death or he will give it to anybody whom in my will I will ask to give. The final right on the estate will be mine but you can spend Rs. 600 as you like and if there is any extra income you can utilise it for anything you wish to buy, *e.g.*, household utensils etc. After your death the said capital will be mine or it will be given to whom I may ask in my will to give. You have no right whatsoever to give the amount to anybody not even your heirs. You should act according to my wishes up to the end of my life and you should serve me. If I am displeased with your conduct or actions you have no right to take the matter to any Court for disproving it. I have preserved the right to use the capital as I like by making any arrangement I like. I have not kept with me the right to make any changes in that arrangement or to cancel it."

Now it appears that no specific assets were set aside to meet this sum of Rs. 20,000 and that there are no further entries in the books with regard

to it. The first question which we have to consider is, what is the correct construction to be put upon this document? In my judgment it is clearly irrevocable, *i.e.*, the covenanted sum cannot be revoked by the covenantor at any time. In substance it is a covenant to pay the income of Rs. 20,000 with a guarantee that there shall be Rs. 600 a year, and if there is any additional income that sum is also to be paid over. I do not think it is necessary to determine whether if the lady chose she could sue to have a sum of Rs. 20,000 to be set apart or ear-marked to provide the covenanted annual sum. It is now necessary to examine the relevant provisions of the Income-tax Act, which is Section 16 (1). The section commences with the governing words: "In computing the total income of an assessee"—we are not concerned with sub-clauses (*a*) and (*b*) but sub-clause (*c*) is as follows: "All income arising to any person by virtue of a settlement or disposition whether revocable or not, and whether effected before or after the commencement of the Indian Income-tax (Amendment) Act, 1939, from assets remaining the property of the settlor or disponer, shall be deemed to be income of the settlor or disponer, and all income arising to any person by virtue of a revocable transfer of assets shall be deemed to be income of the transferor." Then there follow three provisos to that sub-section, the first of which we are not concerned with as it relates to the transfer of assets. The second is a definition clause and it provides that "the expression 'settlement or disposition' shall for the purposes of this clause include any disposition, trust, covenant, agreement, or arrangement, and the expression 'settlor or disponer' in relation to a settlement or disposition shall include any person by whom the settlement or disposition was made." Now turning back for a moment to the main sub-clause (*c*) it is to be observed that it applies to all income arising to any person by virtue of a covenant whether revocable or not, from assets remaining the property of the settlor or disponer. Now in my judgment that is the position created by this entry in the assessee's books. If that is so then it falls to be considered whether the position is taken out of the main sub-clause (*c*) by the third proviso which is as follows: "Provided further that this clause shall not apply to any income arising to any person by virtue of a settlement or disposition which is not revocable for a period exceeding six years or during the lifetime of the person and from which income the settlor or disponer derives no direct or indirect benefit but that the settlor shall be liable to be assessed on the said income as and when the power to revoke arises to him." As I have stated this entry is an irrevocable covenant and it therefore comes within the third proviso unless it can be said that this is income from which the assessee derives a direct or indirect benefit. It is no doubt true that a husband is under an obligation to maintain his wife but it cannot be suggested that this entry is in fulfilment of any such obligation. By the words used the wife is enabled to do what she likes

with the covenanted annual sum of Rs. 600. She can either accumulate the same, or she can hand it over to her own parents. There is no obligation on her either to maintain herself or to spend it in buying necessary utensils for the household. In these circumstances in my opinion this is not a benefit either direct or indirect which the assessee derives from this covenant and in my judgment the position falls within the third proviso to sub-clause (c) of sub-section (1) of Section 16 of the Income-tax Act. Accordingly in my judgment the answer to the question submitted to the Court is in the negative. The Commissioner must pay the costs of the reference taxed on the original side scale.

KANIA, J.—I agree. The relevant portions of the entry, under which the rights of the parties have to be determined, have been quoted in the judgment of the learned Chief Justice. The question submitted for the Court's opinion is whether the income of Rs. 280 arising from assets, which, on the construction of this entry, are considered to remain the property of the assessee, is liable to be assessed as the income of the assessee.

There appears no doubt that the capital amount of Rs. 20,000 mentioned in the entry, at no time, ceased to be property of the assessee. By the entry also he has not transferred a specific amount to himself in another capacity. In law, therefore, it would be proper to state that there is no transfer of assets by the settlor to another party. The question for consideration is whether on the facts found by the Tribunal the income remains the income of the assessee. It is common ground that Section 16 (1) (c) of the Act applies. The first part of that clause deals with income arising to any person by virtue of a settlement or disposition, whether revocable or not, from assets remaining the property of the settlor or disponer. According to the first part of that clause such income shall be deemed to be the income of the settlor or disponer. The second part of the clause deals with income arising to any person by virtue of a revocable transfer of assets. The clause provides that such income shall be deemed to be the income of the transferor. This is the substantive part of clause (c). It is followed by the first proviso which extends the meaning of what is a revocable transfer of assets mentioned in the second part of the clause. In this reference we are not concerned with that proviso. The second proviso states that the expression "settlement or disposition" shall, for the purposes of this clause, include any disposition, trust, covenant, agreement or arrangement. The words "settlement or disposition" used in the first part of clause (c) are thus given an extended meaning. Therefore, although there may be no trust as defined by the Trusts Act, if there is a covenant, agreement or arrangement which fulfils the conditions mentioned in the clause, such a covenant, agreement or arrangement is covered by Section 16 (1) (c). The question therefore arises whether the third proviso applies to the arrangement contained in the entry in question.

On behalf of the Commissioner it was urged that the third proviso is not applicable unless there was a transfer of assets. In support of that contention reliance was placed in particular on the last words of the proviso, *viz.*, "the settlor shall be liable to be assessed on the said income as and when the power to revoke arises to him." From these words it was sought to be argued that the power to revoke must be a revocation of the transfer of assets. In my opinion this argument is unsound. The proviso opens with the words "Provided further that this clause shall not apply..." There is no warrant for reading the word "clause" as applicable only to the second half of clause (*c*), and not the first half also. In my opinion, the last words of the proviso, quoted above, also do not help the Commissioner, because the power to revoke may be equally applicable to the income, which is payable, as to the assets which are transferred. In proviso (1) the transfer of income and assets are treated, so far as this section is concerned, on the same footing. It appears therefore that the third proviso, as worded, can equally well apply to the first part of Section 16 (1) (*c*). It was next argued that having regard to the words "revocable or not" used in the first part of clause (*c*), the third proviso cannot apply until there was a revocable transfer of assets. No authority is cited to support this construction, which is against the very words of the clause. The words "revocable or not," in my opinion, are used in contradiction to "revocable transfer" used in the second part of that clause. Although the settlement may be revocable, the power may not be capable of being exercised for a period exceeding six years, or for the lifetime of the person for whose benefit the income is settled. The deed may not be revocable and yet the settlor may derive a benefit directly or indirectly from the income. The use of the words "revocable or not" in the first part of Section 16 (1) (*c*) does not therefore necessarily exclude the operation of the third proviso. In my opinion, therefore, the argument that before the third proviso can be considered, the settlement must be revocable, is unsound.

The next question for consideration is whether the arrangement contained in the entry satisfied the conditions prescribed in the third proviso. In terms, the entry says that the settlement shall not be revoked or altered. It, therefore, makes the deed irrevocable during the lifetime of the assessee's wife, for whose benefit the arrangement is made. The first condition of the third proviso is thus fulfilled. The second condition is that "from the income (so settled on the wife during her lifetime) the settlor derives no direct or indirect benefit." On a perusal of the entry, which embodies the arrangement, it is clear that the settlor has no power of disposition over the income. The wife is entitled to utilise it as she pleases, irrespective or in total disregard of the wishes or desires of the assessee. It was contended that the assessee is bound to maintain his wife and this income, which

is settled on her, may be taken into consideration if she claimed separate maintenance. The question does not arise on the reference directly. The argument is that a husband being under a legal obligation to maintain his wife, if he settles property for her exclusive and independent maintenance (and although he has no control over it thereafter) it amounts to a receipt of indirect benefit by the husband. This argument was advanced in Income-tax Reference No. 20 of 1943* and rejected by the Court. In my opinion, the assessee derives no direct or indirect benefit under this arrangement, within the meaning of the third proviso.

In their judgment the Tribunal has considered that the third proviso does not apply to the first part of Section 16 (1) (*c*) and therefore have not expressed any opinion on that aspect of the case. In my opinion the construction put by them is incorrect and not warranted by the words of this proviso. I therefore agree that the answer to the question, submitted to the Court, should be in the negative.

Reference answered in the negative.

[IN THE OUDH CHIEF COURT.]

RANI TARA KUMARI DEVI

v.

COMMISSIONER OF INCOME TAX, U. P., C. P. AND BERAR.

BENNETT and MADELEY, JJ. November 23, 1944.

INDIAN INCOME-TAX ACT (XI OF 1922), SECS. 2 (1) & 4 (3) (*viii*)—AGRICULTURAL INCOME—INCOME FROM SALE OF FOREST TREES AND WILD GRASS OF SPONTANEOUS GROWTH.

Income from the sale of forest trees and wild grass of spontaneous growth, growing on land naturally and without the intervention of human agency, is not agricultural income within the meaning of Section 2 (1) of the Income-tax Act even if such land is assessed to land revenue, and such income is not exempt from income-tax under Section 4 (3) (viii) of the Act.

MAHARAJA OF KAPURTHALA *v.* COMMISSIONER OF INCOME-TAX, CENTRAL AND UNITED PROVINCES [1945] (13 I.T.R. 74; 1944 O.W.N. 443) *followed.*

Reference under Section 66 (1) of the Indian Income-tax Act (XI of 1922) by the Income-tax Appellate Tribunal: (Civil Reference under Income-tax Act No. 5 of 1943).

M. H. Qidwai, for the assessee.

S. C. Dass, for the Commissioner.

JUDGMENT.

This is a reference by the Income-tax Appellate Tribunal under Section 66 (1) of the Indian Income-tax Act.

* Since reported as *Ramji Keshavji* v. *Commissioner of Income-tax, Bombay* [1945] 13 I.T.R. 105.

The assessee is Rani Tara Kumari Devi, Majhgain Estate, District Kheri, widow of the taluqdar of that estate. She was assessed for the year 1941-42 upon her income from various sources including forest trees and wild grass and the question referred by the Tribunal on her application is :—

" Whether income from the sale of forest trees and wild grass of spontaneous growth growing on land, which is assessed to land revenue, naturally and without the intervention of human agency, is 'agricultural income' within the meaning of Section 2 (1) of the Income-tax Act, and as such exempt from income-tax under Section 4 (3) (*viii*) of the Act?"

As regards the sale of forest trees so growing the question was considered on a similar reference in *Maharaja of Kapurthala* v. *Commissioner of Income-tax, Central and United Provinces*[1], in which case we held that income derived from the sale of such trees is not agricultural income and therefore not exempt from income-tax under Section 4 (3) (*viii*).

We are unable to hold that the sale of wild grass of spontaneous growth stands on a different footing. We considered in the case cited the effect of the exclusion of timber from the head of "sewai" income and expressed agreement with the Tribunal that "the question whether income from some sources only (such as lac, honey, wax and fruit) is taken into consideration in the land revenue settlement and income from other sources, such as sales of timber, excluded is irrelevant." It is therefore in our opinion immaterial whether income from such sources has been included under the head of "sewai" income in assessing the land to land revenue. We can see no reason why a different principle should be applied to the case of wild grass, and we accordingly answer the question by saying that income from the sale of forest trees and wild grass of spontaneous growth growing on land, which is assessed to land revenue, naturally and without the intervention of human agency is not "agricultural income" within the meaning of Section 2 (1) of the Income-tax Act, and not therefore exempt from income-tax under Section 4 (3) (*viii*) of the Act.

The assessee will pay the costs of this reference. We fix the fee of the learned counsel for the Income-tax Department at Rs. 100.

Reference answered accordingly.

[IN THE OUDH CHIEF COURT.]

RAJA PRATAP BIKRAM SHAH

v.

COMMISSIONER OF INCOME-TAX, U. P., C. P. AND BERAR.

MADELEY and WALFORD, JJ. April 12, 1946.

INDIAN INCOME-TAX ACT (XI OF 1922), SECS. 2 (1) & 4 (3) (*viii*)—AGRICULTURAL INCOME—INCOME FROM SALE OF FOREST TREES, WILD GRASS AND

(1) [1945] 13 I.T.R. 74 ; 1944 O.W.N. 443.

FRUITS OF TREES GROWING ON LAND NATURALLY AND SPONTANEOUSLY—WHETHER AGRICULTURAL INCOME.

Income from the sale of (i) catechu, (ii) Kah-charai *(dues paid for grazing wild grass), (iii)* Narkul Jalkar *(reeds growing on banks of rivers), (iv) forest timber, (v) grass,* phus *(thatching straw) and* bhang *and (vi) fruits of mango,* imli *(tamarind) and* kathal *(jack fruit) trees which have grown on land naturally and spontaneously and without the intervention of human agency is not agricultural income within the meaning of Section 2 (1) of the Indian Income-tax Act, even if such land is assessed to land revenue, and such income is not exempt from income-tax under Section 4 (3) (viii) of the Act.*

Cases referred to :—

Chandrasekhara Bharati *v.* Duraiswami Naidu [1931] (I.L.R. 54 Mad. 900; 134 I.C. 42; A.I.R. 1931 Mad. 659).

Commissioner of Income-tax, Madras *v.* T. Manavedan Tirumalpad [1930] (I.L.R. 54 Mad. 21; 126 I.C. 596; A.I.R. 1930 Mad. 764; 4 I.T.C. 421).

Kesho Prasad Singh *v.* Sheo Pragash Ojha [1922-24] (I.L.R. 44 All. 19; 64 I.C. 248; A.I.R. 1922 All. 301; on appeal to Privy Council I.L.R. 46 All. 831; 82 I.C. 962; A.I.R. 1924 P.C. 247; 51 I.A. 381).

Maharaja of Kapurthala *v.* Commissioner of Income-tax, Central and United Provinces [1945] (13 I.T.R. 74; 20 Luck. 212; 1944 O.W.N. 443; A.I.R. 1945 Oudh 35).

Province of Bihar *v.* Maharaja Pratap Udai Nath Sahi Deo of Ratugarh [1941] (9 I.T.R. 313; 194 I.C. 203; A I.R. 1941 Pat. 289; 20 Pat. 699)

Rani Tara Kumari Devi, Majhgain Estate *v.* Commissioner of Income-tax, U. P., C. P. and Berar [1946] (14 I.T.R. 787).

Special Manager, Court of Wards *v.* Commissioner of Income-tax, C. P. & U P. [1945] (13 I.T.R. 94; A.I.R. 1945 Oudh 42; 1944 O.W.N. 451).

Reference under Section 66 (1) of the Indian Income-tax Act (XI of 1922) by the Income-tax Appellate Tribunal: (Civil Reference No. 1 of 1944).

R. N. Sinha, for the assessee.

S. C. Dass, for the Commissioner.

JUDGMENT.

This is a reference under Section 66 (1) of the Indian Income-tax Act on an application by the assessee Rani Subhadra Devi Sahiba of Khairgarh Raj, District Kheri. Rani Subhadra Devi has died and Raja Pratap Bikram Shah has been brought on the record as her legal representative.

The Income-tax Officer had included certain items of revenue in computing the total income of the assessee for the year 1941-42 to which the assessee objected as being revenue derived from land which was used for agricultural purposes and which is assessed to land revenue within the meaning of Section 2 (1) of the Income-tax Act and was, therefore, exempt from assessment to income-tax under Section 4 (3) (*viii*). The items in dispute were:

(*i*) Sale of catechu, Rs. 5,095.

(*ii*) *Kah-charai* (dues paid for grazing wild grass), Rs. 3,350.

(*iii*) Sale of *Narkul Jalkar* (thin reeds growing on the banks of a river), Rs. 1,485.

(*iv*) Sale of forest timber, Rs. 6,856.

(*v*) (*a*) Sale of grass and *phus* (thatching straw), *jhau* (a kind of shrub growing on the banks of a river).

(*b*) Income from *bhang* (rent paid to assessee by persons holding a licence for taking settlement of *bhang* plants), Rs. 1,755.

(*vi*) Sale of mango, *imli* and *kathal* fruits, Rs. 1,419.

The Income-tax Officer came to the conclusion that the receipts in question were taxable as the land from which the income was derived was not used for agricultural purposes, even though it was assessed to land revenue. The decision of the Income-tax Officer was affirmed by the Appellate Assistant Commissioner, and upon a further appeal to the Income-tax Appellate Tribunal, the decisions of the Income-tax Officer and the Appellate Assistant Commissioner were upheld.

Being dissatisfied, the assessee made an application to the Income-tax Appellate Tribunal to make a reference to this Court under Section 66 (1) of the Income-tax Act. The question formulated by the Tribunal and referred to this Court is :

"Whether in the circumstances of the present case income from the sale of (*i*) catechu, (*ii*) *Kah-charai*, (*iii*) *Narkul Jalkar*, (*iv*) forest timber, (*v*) (*a*) grass and *phus* and (*b*) *bhang* and (*vi*) fruits of mango, *imli* and *kathal* trees (all of which have grown on the land naturally and spontaneously and without the intervention of any human agency), even if such land is assessed to land revenue, is agricultural income, within the meaning of Section 2 (1) of the Income-tax Act and as such exempt from income-tax under Section 4 (3) (*viii*) of the Act."

The Appellate Tribunal in deciding the appeal has relied upon principles laid down in a number of decisions of various High Courts for the proposition that the items in dispute, being of wild and spontaneous growth, did not come within the meaning of Section 2 (1) of the Income-tax Act, and were consequently assessable to income-tax and we are of the opinion that the conclusions at which the Tribunal has arrived are correct.

It is now settled law that the income from sale of forest trees or fruit from trees which are of spontaneous growth on land, even if it is assessed to land revenue, is not income from land used for agricultural purposes.

In *Chandrasekhara Bharati* v. *Duraiswami Naidu*[1], a Division Bench of the Madras High Court held that growing trees for fuel is not an agricultural purpose so as to make a person, who holds the land for that purpose, a *raiyat* within the meaning of the Madras Estates Land Act. In this

(1) (1931) I.L.R. 54 Mad. 900

case Reilly, J., observed, and which observation has been quoted with approval by a Bench of this Court, to which we shall presently refer, as follows:

"If we take the strict meaning of 'agriculture' according to its derivation, it means the cultivation of a field, the cultivation of an open space as opposed to horticulture, the cultivation of a comparatively small enclosed space......But the planting of timber or fire wood trees, which are to stand on the land for a considerable number of years forming plantations or woods or forests, appears to me to be opposed to the idea of agriculture, the cultivation of an open space. It is true that for the purpose of growing trees in a plantation it may be necessary first to prepare the land. Later on it may be necessary to protect and water the young plants. Still later it may be necessary to thin out the plantation. But when the land is covered with trees which have to stand on it for a number of years, sometimes as long as a century, during most of which period the land itself is untouched, to describe that as agriculture appears to me inappropriate. To my mind, it seems to be different from the cultivation of a field or of an open space."

The next case referred to by the Appellate Tribunal is *Commissioner of Income-tax, Madras* v. *T. Manavedan Tirumalpad*[1], wherein a Special Bench held that:

"The amounts received by the owner of unassessed forest lands, by the sale of timber trees thereon, are income liable as such to income-tax."

In *Province of Bihar* v. *Maharaja Pratap Udai Nath Sahi Deo of Ratugarh*[2], which was a decision by a Special Bench of the Patna High Court, Harries, C. J., made the following observations:

"It appears that this head of income was derived from virgin jungles or jungle land not actually cultivated. A few forest guards appear to have been employed to protect the property, but it cannot be said that the trees have grown as the result of cultivation. They appear to have grown naturally in the jungles without the intervention of human agency, and in my view, the growth of these trees cannot be said to result from the cultivation of the soil. In fact, it was the absence of cultivation that permitted the area to develop into a jungle."

Similar view was taken by a Bench of this Court to which one of us was a party. In *Maharaja of Kapurthala* v. *Commissioner of Income-tax, Central and United Provinces*[3], after reviewing the case law exhaustively, the Bench of this Court held that

"Income from the sale of forest trees of spontaneous growth growing on land which is assessed to land revenue is not agricultural income within the meaning of Section 2 (1) (*a*) of the Income-tax Act and is not exempt from income-tax under Section 4 (3) (*viii*) of the Act."

(1) (1930) I.L.R. 54 Mad. 21.
(2) [1941] 9 I.T.R. 313.
(3) [1945] 13 I.T.R. 74.

We may also refer to *Special Manager, Court of Wards* v. *Commissioner of Income-tax, C.P. & U.P.*[1], which was decided on the same principle.

In view of the decisions cited above, it can no longer be argued that income from sale of trees of spontaneous growth comes within the definition of agricultural income or income from land used for agricultural purposes.

With regard to the other items in dispute, which are also of spontaneous growth, the principles laid down in the above authorities relating to forest trees of spontaneous growth are applicable with equal force. In *Kesho Prasad Singh* v. *Sheo Pragash Ojha*[2], a Full Bench of the Allahabad High Court held that the land used for the purpose of a grove was not land held for agricultural purpose. This decision was approved by their Lordships of the Judicial Committee in *Kesho Prasad Singh* v. *Sheo Pragash Ojha*[3]. If, therefore, a grove in which mango, *imli* and *kathal* fruit trees usually grow, is not land held for agricultural purposes, it follows that income from the fruits of such trees in a grove is not agricultural income and *a fortiori* income from the fruits of trees of spontaneous growth cannot be held to be such income as to be exempt from income-tax under Section 4 (3) (*viii*) of the Income-tax Act.

The learned counsel for the applicant has strenuously contended that the grass growing on land, which is used by the agriculturists for grazing their cattle and which, according to him, forms part of agriculture, or *phus* and *jhau* which are used indirectly for agricultural purposes, the land upon which such grass or *phus* or *jhau* grow should be deemed to be land used for agricultural purposes. There is, in our opinion, a fallacy in this contention. If income from sale of commodities which agriculturists use in order to carry on their trade or business were to be included in the definition of agricultural income, a large number of manufacturers and traders will necessarily be exempted from income-tax. For example, the manufacturers of implements of husbandry and innumerable other manufacturers and traders, who cater for agriculturists, would claim exemption from income-tax on the ground that the commodities they produce and sell to agriculturists are agricultural income. We have given these examples to show the absurdity to which the question can be reduced. The learned counsel has attempted to draw a distinction between sale of grass and the income derived from grazing dues, but we are unable to see any difference between the two. In an unreported case, *Rani Tara Kumari Devi, Majhgain Estate, District Kheri* v. *Commissioner of Income-tax, U.P., C.P. and Berar, Lucknow* (Civil Reference under Income-tax Act No. 5 of 1943)* on a question: "Whether income from the sale of forest trees and wild grass of

(1) [1945] 13 I.T.R. 94.
(2) (1922) I.L.R. 44 All. 19.
(3) (1924) I.L.R. 46 All. 831.

* Since reported at page 787 *supra*.

spontaneous growth growing on land, which is assessed to land revenue, naturally and without the intervention of human agency, is 'agricultural income' within the meaning of Section 2 (1) of the Income-tax Act, and as such exempt from income-tax under Section 4 (3) (*viii*) of the Act?" a Bench of this Court, to which one of us was a party, held that the income from sale of such grass did not come within the exemption provided by Section 4 (3) (*viii*) of the Income-tax Act. As already observed, we see no difference between the revenue derived by the sale of grass or by way of grazing dues.

Upon consideration of the authorities cited above, we are of the opinion that none of the items in dispute in the present case are exempt from income-tax and we answer the question referred to us accordingly.

The assessee will pay the costs of this reference. We fix the fee of the learned counsel for the Income-tax Department at Rs. 100.

Reference answered accordingly.

[IN THE BOMBAY HIGH COURT.]

COMMISSIONER OF INCOME TAX, BOMBAY

v.

NAROTTAM PEREIRA LTD., BOMBAY.

SIR LEONARD STONE, C. J., and CHAGLA, J. August 17, 1946.

EXCESS PROFITS TAX ACT (XV OF 1940), SECS. 2 (10) & (21) (*a*), R. 7 (1), SCH. I—DIRECTOR CONTROLLED COMPANY—HOLDING OF MAJORITY OF SHARES BY DIRECTORS, NECESSITY OF—SHAREHOLDER OWNING NOT LESS THAN 20 PER CENT. OF SHARES APPOINTING NOMINEES AS DIRECTORS—WHETHER A "DIRECTOR."

Before a controlling interest within the meaning of Section 2 (21) (a) and rule 7 (1) of Schedule I of the Excess Profits Tax Act can be established the directors *must hold a majority of the shares in the company.*

Out of the 60 ordinary shares in the assessee company, 21 shares were held by seven directors. Three of these directors, who held 3 shares in all, were the nominees of a navigation company which held 20 shares and thereby was the beneficial owner of not less than 20 per cent. of the ordinary share capital of the company within the meaning of Section 2 (10) of the Excess Profits Tax Act. It was contended that the navigation company was a real director and as such the assessee company was a company in which the directors had a controlling interest :

Held, *that the navigation company was not a director within the meaning of Section 2 (10) of the Excess Profits Tax Act and that the assessee company was not therefore a company in which the directors had a*

controlling interest within the meaning of Section 2 (21) (a) and Rule 7 (1) of Schedule I of the Act.

Reference under Section 21 of the Excess Profits Tax Act (XV of 1940) read with Section 66 (1) of the Indian Income-tax Act (XI of 1922) by the Income-tax Appellate Tribunal: (Income-tax Reference No. 4 of 1945.)

STATEMENT OF CASE.

" This is an application under Section 21 of the Excess Profits Tax Act read with Section 66 (1) of the Indian Income-tax Act, by the Commissioner of Income-tax, Bombay, requiring the Tribunal to refer to the High Court of Judicature at Bombay a question of law arising out of the order of the Tribunal in 14 (1) E.P.T.A.A. No. 53-(Bombay) of 1943-44.

2. While making the excess profits tax assessment for the chargeable accounting period from 1st July, 1940, to 30th June, 1941, the Excess Profits Tax Officer examined the assessee's claim to the effect that the directors of the assessee company had a controlling interest therein within the meaning of Section 2 (21) (*a*) of the Excess Profits Tax Act and Rule 7 (1) of Schedule I to the said Act and came to the conclusion that the directors did not have a controlling interest in the assessee company within the meaning of the two above-mentioned provisions, during the accounting period. An appeal was preferred to the Appellate Assistant Commissioner but was unsuccessful. The assessee then came up in appeal to the Tribunal. The Tribunal found that out of the eight persons who were directors of the company during the accounting period, seven were nominated directors under articles 89 and 90 of the appellant company's articles of association, which articles are set out in extenso in the Tribunal's order. The Tribunal found that out of a total of 60 ordinary shares issued by the company which alone carry voting rights, the voting rights in respect of 50 shares were exercised subject to the will and ordering of the directors. As a result of the above-mentioned findings the Tribunal concluded that the directors of the assessee company had a controlling interest therein within the meaning of Section 2 (21) (*a*) of the Excess Profits Tax Act and Rule 7 (1) of Schedule I to that Act. The Tribunal relied upon the decision in *British American Tabacco Co.* v. *Inland Revenue Commissioners*[1], and was of the opinion that the term 'controlling interest' had a much wider connotation and cannot, in its meaning, be restricted to a proprietary right or a bare beneficial interest as was contended on behalf of the Department. The facts of the case are mentioned in detail in the Tribunal's order and the material upon which the findings have been based is also contained therein. The dispute really turned upon the 24 shares held by the Scindia Steam Navigation Co., Ltd., and nine shares held by Mrs. Nanavati. The Scindia Steam Navigation Co., Ltd., had three nominees as directors while

(1) [1943] 11 I.T.R. Suppl. 29.

Mrs. Nanavati had nominated one director. Both these shareholders filed certificates before the Tribunal to the effect that the voting rights in respect of their share holdings were always exercised in accordance with the advice of their nominee directors. These certificates were not questioned by the Departmental Representative and were accepted by the Tribunal as representing the true state of affairs. The 33 shares belonging to the Scindia Steam Navigation Co., Ltd., and Mrs. Nanavati added to the 17 shares which were held by the directors in their own names during the year of account made up 50 out of the total ordinary share capital issue of 60 shares.

3. The applicant points out that the order of the Tribunal involves the interpretation of the term 'controlling interest' occurring in Section 2 (21) (*a*) of the Excess Profits Tax Act and in Rule 7 (1) of Schedule I to the said Act. We agree that a question of law arises since the Tribunal's decision has turned upon the interpretation of that expression and we refer the following question to the High Court of Judicature at Bombay under Section 21 of the Excess Profits Tax Act read with Section 66 (1) of the Indian Income-tax Act.

'Whether, upon the facts found by the Tribunal, the assessee company is one in which the directors had a controlling interest within the meaning of Section 2 (21) (*a*) of the Excess Profits Tax Act and Rule 7 (1) of Schedule I to that Act.' "

This reference came before Sir Leonard Stone, C. J., and Kania, J., on 19th September, 1945, and the reference was sent back to the Tribunal for a further statement of case.

The supplementary statement of case submitted by the Appellate Tribunal was as follows:—

SUPPLEMENTARY STATEMENT OF CASE.

" The Appellate Tribunal has been directed under Section 66 (4) of the Indian Income-tax Act by the High Court of Judicature at Bombay to record its findings on the following questions:—

(1) Who are the directors of the respondent company?

(2) What is the interest in fact of each of the directors in the respondent company? and

(3) Whether the Scindia Steam Navigation Company Limited and/or Mrs. Navavati are the directors of the respondent company as contended by the respondent assessee?

Our findings are as follows:—

(a) (1) Mr. P. N. Vevaina, (2) Dewan Bahadur I. X. Pereira, (3) Mr. J. E. A. Pereira, (4) Mr. Walchand Hirachand, (5) Mr. Shantikumar N. Morarji, (6) Sir Chunilal B. Mehta, (7) Honourable Sir Shantidas Askuran, and (8) Mr. S. C. Sheth.

(b) The number of shares held by the above directors are as follows:—

(1) Mr. P. N. Vevaina	...	9 shares
(2) Dewan Bahadur I. X. Pereira	...	5 shares
(3) Mr. J. E. A. Pereira	...	3 shares
(4) Mr. Walchand Hirachand	...	1 share
(5) Mr. Shantikumar N. Morarji	...	1 share
(6) Sir Chunilal B. Mehta	...	1 share
(7) Honourable Sir Shantidas Askuran	...	1 share.

It may, however, be stated that the four shares held by (1) Mr. Walchand Hirachand, (2) Sir Chunilal B. Mehta, (3) Honourable Sir Shantidas Askuran and (4) Mr. Shantikumar N. Morarji are the property of the Scindia Steam Navigation Company Limited.

(c) Neither the Scindia Steam Navigation Company Limited nor Mrs. Maniben C. Nanavati is a director of the respondent company.

2. It is contended by Sir Jamshedji on behalf of the respondent company that Mr. Walchand Hirachand, Sir C. B. Mehta and Honourable Sir Shantidas Askuran are not the directors of the company; but that in their place the Scindia Steam Navigation Company Limited is the director. It is also contended by him that Mr. S. C. Sheth is not a director and that in his place Mrs. Nanavati is the director. It is, however, admitted that the names, as given by us, are on the register of the company. The contention of Sir Jamshedji is that the Scindia Steam Navigation Company Limited and Mrs. Nanavati are virtually the directors. The fact that the Scindia Steam Navigation Company Limited and Mrs. Nanavati have the right to nominate directors does not mean that they are either *de facto* or *de jure* directors. Mr. Walchand Hirachand, Sir C. B. Mehta and Honourable Sir Shantidas Askuran have been nominated by the Scindia Steam Navigation Company Limited and Mr. S. C. Sheth was nominated by Mrs. Nanavati. Our attention was drawn by the learned counsel to the definition of 'director' in Section 2 (10) of the Excess Profits Tax Act. That section runs as follows—

"'director' includes any person occupying the position of a director by whatever name called and also includes any person who—

(i) is a manager of the company or concerned in the management of the business;

(ii) is remunerated out of the funds of the business; and

(iii) is the beneficial owner of not less than twenty per cent. of the ordinary share capital of the company."

It is contended that the Scindia Steam Navigation Company Limited and Mrs. Nanavati are concerned in the management of the business of the respondent company. It is doubtful whether a person who has a power to

nominate a director can be said to be concerned in the management of the company. But assuming that it is so, the question still remains whether the Scindia Steam Navigation Company Limited and Mrs. Nanavati satisfy the other two tests laid down in Section 2 (10). In order that a person may be a director, he must be—

(1) A manager of the company or be concerned in the management of the business;

(2) remunerated out of the funds of the business; and

(3) the beneficial owner of not less than twenty per cent. of the ordinary share capital of the company.

All the three conditions have to be satisfied. There is no material on record to show that the Scindia Steam Navigation Company Limited is remunerated out of the funds of the respondent company. What is stated is that fees are paid by the company to the nominees of the Scindia Steam Navigation Company Limited and Mrs. Nanavati under article 93 of the articles of association of the company. It is not even suggested that the fees paid to the directors, that is to say to the nominees under article 93, are handed over by the nominees to their nominators. In the case of Mrs. Nanavati the third test is not satisfied, because she is not the beneficial owner of not less than 20 per cent. of the ordinary share capital of the respondent company. She holds only nine shares out of the total of 60 shares. In the case of the Scindia Steam Navigation Company Limited, it holds 20 shares and four more, if it be held that the shares in the names of Mr. Walchand Hirachand, Sir C. B. Mehta, Honourable Sir Shantidas Askuran and Mr. Shantikumar N. Morarji are the shares of the Scindia Steam Navigation Company Limited. The Scindia Steam Navigation Company Limited does satisfy the third test."

M. C. Setalvad, for the Commissioner.

Sir Jamshedji Kanga and *R. J. Kolah*, for the assessee.

JUDGMENT.

CHAGLA, J.—The question raised by the Tribunal on this reference is whether, upon the facts found by the Tribunal, the assessee company is one in which the directors had a controlling interest within the meaning of Section 2 (21) (*a*) of the Excess Profits Tax Act and rule 7 (1) of Schedule I to that Act.

This reference came before me and my learned brother Mr. Justice Kania on the 19th September, 1945, and we sent the reference back to the Tribunal under Section 66 (4) of the Act and requested them to record their findings on the three questions which we raised. The three questions were:—

(1) Who are the directors of the respondent company?

(2) What is the interest in fact of each of the directors in the respondent company? and

(3) Whether the Scindia Steam Navigation Company Limited and/or Mrs. Nanavati are the directors of the respondent company as contended by the respondent assessee?

The supplementary statement of the Tribunal is now before us and they have answered the three questions raised by us. Their findings are that Mr. P. N. Vevaina, Dewan Bahadur I. X. Pereira, Mr. J.E.A. Pereira, Mr. Walchand Hirachand, Mr. Shantikumar N. Morarji, Sir Chunilal B. Mehta, the Honourable Sir Shantidas Askuran and Mr. S. C. Sheth are the eight directors of the assessee company. They have also stated that the number of shares held by the directors are as follows:—

Mr. P. N. Vevaina	...	9 shares
Dewan Bahadur I. X. Pereira	...	5 shares
Mr. J. E. A. Pereira	...	3 shares
Mr. Walchand Hirachand	...	1 share
Mr. Shantikumar N. Morarji	...	1 share
Sir Chunilal B. Mehta	...	1 share
Honourable Sir Shantidas Askuran	...	1 share

So it will be found that the shares held by these seven directors total 21 shares. The total ordinary shares of the company are 60 and therefore on this finding, out of the 60 ordinary shares 21 shares are held by the directors. As the finding stands, there can be no question that these directors have no controlling interest in the company. Before a controlling interest can be established, the directors must hold a majority of the shares and when the Tribunal has found that the directors hold only 21 out of 60 shares it is impossible to contend that the directors have a controlling interest.

To get over this almost insuperable difficulty Sir Jamshedji has advanced a rather ingenious argument. What he says is this, that the Scindia Steam Navigation Company hold 20 shares and they have nominated Mr. Walchand Hirachand, Sir Chunilal Mehta and Honourable Sir Shantidas Askuran as the nominees. Therefore, these three nominees are not the real directors, but the real director is the Scindia Steam Navigation Company and as such the Scindia Steam Navigation Company controls 20 shares. This argument is based on the contention that as it is not possible for a limited company to be a director of another company, therefore, the Scindia Steam Navigation Company was compelled to nominate these three gentlemen as the directors.

Now, Sir Jamshedji Kanga has cited no authority for this proposition that a limited company cannot be appointed a director of another company and in the absence of any such authority we are not prepared to accept that statement of the law as a correct statement.

It has also been contended by Sir Jamshedji Kanga that the Scindia Steam Navigation Company comes under the definition of "director" given in Section 2 (10). That definition, it is true, is not exhaustive but an inclusive definition and it provides that a "director" includes any person occupying the position of a director by whatever name called and also includes any person who (1) is a manager of the company or concerned in the management of the business; and (2) is remunerated out of the funds of the business; and (3) is the beneficial owner of not less than 20 per cent. of the ordinary share capital of the company.

Now, it is true that the Scindia Steam Navigation Company is the beneficial owner of not less than 20 per cent. of the ordinary shares of the company, but I fail to see how it can be said that the Scindia Steam Navigation Company is the manager of the company or concerned in the management of the business or that it is remunerated out of the funds of that business. In order that this definition can apply, all the three conditions which are cumulative must be satisfied. It is also rather significant to note that in the certificate which was filed by the Scindia Steam Navigation Company before the Tribunal their contention was that the Scindia Steam Navigation Company always voted according to the advice and suggestion of their nominees. Sir Jamshedji Kanga is indeed hard put to it now to suggest entirely the opposite of what is contained in the certificate. The suggestion now is that the nominees really voted at the advice and suggestion of the Scindia Steam Navigation Company. We are therefore of the opinion that the question referred to us by the Tribunal should be answered in the negative. The assessee must pay the costs of the reference.

Reference answered in the negative.

[IN THE CHIEF COURT OF OUDH.]

GOBARDHAN DAS RADHEY LAL

v.

COMMISSIONER OF INCOME-TAX, U.P., C.P. AND BERAR.

MADELEY and WALFORD, JJ. November 22, 1945.

EXCESS PROFITS TAX ACT (XV OF 1940), SECS. 2 (5), SECOND PROVISO, 10 (2), 10A—'PERSON'—WHETHER INCLUDES FIRM—TWO PARTNERS CARRYING ON SAME BUSINESS IN THREE PLACES WITH IDENTICAL SHARES—ADDITION OF ONE PARTNER IN ONE PLACE—ARTIFICIAL TRANSACTION—AVOIDANCE OR REDUCTION OF LIABILITY—IMPOSITION OF PENALTY.

The word "person" in the second proviso to Section 2 (5) of the Excess Profits Tax Act, 1940, includes a firm.

A firm consisting of two partners B and L carried on three business concerns in three places, all dealing in cloth. In all the three concerns B had a twelve annas share and L had a four annas share. Up to 1941-42 returns had been filed on the basis that the three businesses belonged to the same firm. Subsequently B and L took R as a partner in one of the concerns and he was given a one anna share out of the twelve annas share belonging to B. The partnership deed executed on 31st May, 1941, stated that the partnership had commenced from 7th July, 1940. In the 1942-43 income-tax assessment a claim was made that as a new partner was taken in one of the concerns, it was a separate firm and its income should not be amalgamated with the incomes of the other two concerns. The Income-tax Officer held that the partnership deed was bogus and that the three businesses were in fact one firm. The Excess Profits Tax Officer therefore assessed the firm to excess profits tax for the years 1940-41 and 1941-42 on the profits of the three businesses added together and imposed a penalty under Section 10 (2) of the Excess Profits Tax Act. It was found inter alia *that R was the brother-in-law of B and a whole time employee in another company, that he did not bring in any capital, that the alleged change in the constitution of the firm was not notified to the Registrar of Firms as required by Section 63 (1) of the Partnership Act of 1932, and that with the exception of the allocation of profits on the closing day of the year 1941-42, there was no entry in the account books to show that R had been taken in as a partner:*

Held, (*i*) *that the question whether the three businesses were carried on by the same person within the meaning of the second proviso to Section 2 (5) of the Excess Profits Tax Act was a question of fact and a finding on it could only be challenged if the evidence upon which the finding had been arrived at was legally insufficient;*

(*ii*) *that, as the three businesses had been one and the same firm for some years previously, it was for the assessee to prove that they were separate;*

(*iii*) *that there was ample evidence for coming to the conclusion that the partnership deed was bogus and that all the three businesses were carried on by one and the same person,* viz., *the firm consisting of B and L;*

(*iv*) *that the execution of the new deed of partnership was a bogus transaction by which the profits " have been or would be artificially reduced "; the purpose of the transaction was the avoidance or reduction of liability to excess profits tax; the case therefore clearly came under Section 10 (2) and the penalty was legally imposed;*

References under Section 66 (1) of the Indian Income-tax Act (XI of 1922) read with Section 21 of the Excess Profits Tax Act (XV of 1940) by the Income-tax Appellate Tribunal: (Income-tax References Nos. 7 and 9 of 1944 and Application No. 3 of 1944).

STATEMENT OF CASE.

" The assessee firm Gobardhan Das Radhey Lal of Gonda has asked us under Section 66 (1) of the Income-tax Act read with Section 21 of the Excess Profits Tax Act to refer to the Chief Court of Oudh at Lucknow certain questions of law, which, it thinks, arise out of our order under Section 19 of the Excess Profits Tax Act relating to its assessment to excess profits tax for the chargeable accounting period 7th July, 1940, to 25th June, 1941.

2. There are three business concerns, all dealing in cloth, which are carried on by a firm consisting of two partners, Babu Ram and Lallu Mal having Re. 0-12-0 and Re. 0-4-0 shares respectively. The concerns are known as Gobardhan Das Radhey Lal of Colonelganj, District Gonda, Babu Ram Gobardhan Das of Bharwari, District Allahabad and Ram Lakhan Reoti Ram of Bahraich. The records show that since 1936-37 the income, profits and gains of the first two concerns were being assessed to income-tax together in the hands of the applicant firm, Colonelganj being treated as the head office and Bharwari as a branch business. The Bahraich business was started on 13th December, 1937, and its income was included in the applicant firm's income-tax assessment for the first time in 1939-40. Thus the income-tax assessments for 1939-40, 1940-41 and 1941-42 were made on the applicant firm including the income, profits and gains of the three concerns at Colonelganj, Dharwari and Bahraich, Colonelganj being treated as the principal place of business and the other two concerns as the branch businesses. The excess profits tax assessment for the first chargeable accounting period (1st September, 1939, to 6th July, 1940) was also made on the applicant firm taking into consideration the income, profits and gains of all the three businesses named above. It may be stated here that it was not only the case of the department, but also of the applicant firm up to 1941-42 that the three businesses belonged to the same firm of two partners, *viz.*, Babu Ram and Lallu Mal and that Colonelganj was the principal place of business and the other two places mere branches. Returns for several years were also filed on this basis.

3. It was at the 1942-43 income-tax assessment that a claim was made to the effect that a new partner, Raghunath Prasad by name, was taken in in the Bahraich concern, so that it was a separate firm, whose income should not be amalgamated with the income of the other two concerns for the purposes of assessment on the applicant firm. The Income-tax Officer went into the question but considered Raghunath Prasad to be not a *bona fide* partner, holding that the Bahraich concern belonged to the partnership of Babu Ram and Lallu Mal as in the past. He therefore completed the income-tax assessment for 1942-43 as in the past taking into consideration income, profits and gains of all the three concerns. For

the excess profits tax assessment for the 2nd chargeable accounting period, *viz.*, 7th July, 1940, to 25th June, 1941, the Excess Profits Tax Officer adopted the same reasoning as for the income-tax assessment, and computed profits for excess profits tax purposes by considering the income, profits and gains of all the three concerns.

4. It may be made clear here that in the return submitted in connection with this excess profits tax assessment income from the Colonelganj and Bharwari businesses was returned by the applicant firm itself as belonging to the same person, *viz.*, the firm of two partners, Babu Ram and Lallu Mal. But later on in connection with a separate proceeding (under Section 10 (2) of the Excess Profits Tax Act) for the same chargeable accounting period it was claimed that even Colonelganj and Bharwari businesses did not belong to the same firm. When the excess profits tax assessment was taken in appeal before the Appellate Assistant Commissioner, Excess Profits Tax, Cawnpore, the claim was that Bahraich business having an additional partner was a separate firm and that the Colonelganj and Bharwari concerns also did not belong to the same firm, so that the income of the three concerns should not have been added together for purposes of computation of excess profits tax. The learned Appellate Assistant Commissioner however overruled the contentions of the appellant and confirmed the excess profits tax assessment. In doing so, he supported the conclusion of the Excess Profits Tax Officer that Raghunath Prasad was not a *bona fide* partner in the Bahraich concern, and took the three concerns to belong to the same firm. He relied on a U. K. case in which the test was whether there was 'any inter-connection, any inter-lacing, any inter-dependence, any unity at all embracing those two businesses.' He held that this test was fully satisfied in the case of the applicant, so that all the businesses belonged to the same firm.

5. The case was next brought to the Tribunal in second appeal. For reasons mentioned in our order under Section 19 we held that the action of the Excess Profits Tax authorities was correct in view of the second proviso to Section 2 (5) of the Excess Profits Tax Act of 1940 and also in view of the fact that we had no hesitation in agreeing with the Excess Profits Tax authorities that Raghunath Prasad was not a *bona fide* partner in the Bahraich concern.

6. On these facts we have been asked to refer to the Hon'ble Court the following questions of law :—

(A) Whether it was possible in law for the same partners with identical shares to enter into more than one partnership.

(B) Whether there was any evidence to justify the finding that the three businesses, Gobardhan Das Radhey Lal, Gonda, Baburam Gobardhan Das, Bharwari, and Ram Lakhan Reoti Ram, Bahraich, belonged to the same firm.

(C) Whether the three firms noted in question (B) above were the same person within the meaning of Section 2 (5) of the Excess Profits Tax Act and liable to assessment together as such.

(D) Whether in law it is necessary to contribute any capital or services as a consideration for entering into partnership.

7. Under rules 53 and 54 of the Appellate Tribunal Rules the respondent (Commissioner of Excess Profits Tax, U.P. and C.P. and Berar) has submitted a written reply to the application for reference. The learned Commissioner thinks that no question of law arises out of our order under Section 19, but has framed a question, which is noted below, although he thinks that it is essentially a question of fact.

'Whether, in the circumstances of the case, the businesses at Colonelganj (Gobardhan Das Radhey Lal), Bharwari (Babu Ram Gobardhan Das) and Bahraich (Ram Lakhan Reoti Ram) can be said to be *carried on by the same person* (*viz.*, the firm consisting of L. Babu Ram and L. Lallu Mal) within the meaning of the second proviso to Section 2 (5) of the Excess Profits Tax Act.'

8. Dr. Katju appearing in support of the application for reference mentioned a point, which though noted in the grounds of appeal before the Tribunal, was not discussed at the hearing of appeal before us. He pointed out that Gobardhan Das Radhey Lal, Babu Ram Gobardhan Das and Ram Lakhan Reoti Ram had been separately registered as separate firms in the office of the Registrar of Firms. As this point was not discussed before us at the time of the hearing of the appeal, the correctness of the statement was not assessed. But as Dr. Katju says that this is a definite instruction which he received from his client we are prepared to accept the statement. Even then that fact does not seem to be enough or conclusive in the matter of deciding whether the amalgamated assessment of the income, profits and gains of the three concerns was or was not proper under the Excess Profits Tax Act. We are not aware of what check, if any, is exercised by the Registrar of Firms before registering a firm; even if any check is exercised, it is impossible for him to know, without any elaborate enquiry, as to what the real facts are, and we are certain that he has not the means of making such elaborate enquiries. Here we have three concerns which on the applicant's own showing belonged to the same proprietors, one of the places of business being treated as the principal place of business and the other two as the branch business places. Nothing has been shown to induce us to hold that this state of affairs, which was quite a reasonable state of affairs, was altered in the year of account or rather the chargeable accounting period. In order to prove that the three concerns were owned by three separate firms some positive evidence leading to that conclusion should have been adduced, particularly because this conclusion was against the

applicant's own case for some years in the past. No such evidence was however adduced.

9. Question (A), as framed by the applicant in an abstract form, is not fit for reference to the Court. Besides, whether it is possible in law to have more than one partnership with the same partners is a question, which does not arise out of our order—we never said that such a thing was outside the pale of possibility; the real question is what was the position in the present case. Question (D), as mentioned by the learned Commissioner in his written reply, relates to the Bahraich concern. Whether Raghunath Prasad could be regarded as a real partner is a question of fact to be decided with due regard to all the surrounding circumstances of the case. No reference to Court of this abstract question of law or of any other question in this connection is therefore called for. Questions (B) and (C) have been combined by the learned Commissioner into one question; as already mentioned, he considers this to be essentially a question of fact; we think he is right. But this does not, however, exclude, as was urged before us, the possibility of the question being mixed up with a certain question of law relating to the interpretation of the second proviso to Section 2 (5) of the Excess Profits Tax Act read with Section 2 (17) of the same Act. As a matter of fact Dr. Katju in the course of his argument seemed to doubt whether the word 'person' mentioned in the proviso cited above included a firm, although we do not see why there should be such a doubt in view of Section 3 (39) of the General Clauses Act. We are accordingly of the opinion that a question may be referred to the Honourable Court and that it may be framed as below :—

'Whether, in the circumstances of the case, there is any material for holding that the businesses at Colonelganj (Gobardhan Das Radhey Lal), Bharwari (Babu Ram Gobardhan Das) and Bahraich (Ram Lakhan Reoti Ram) are *carried on by the same person* (*viz.*, the firm consisting of L. Babu Ram and L. Lallu Mal) within the meaning of the second proviso to Section 2 (5) of the Excess Profits Tax Act.'

10. In accordance with rule 6 of the Rules for procedure of cases under Section 66 of the Income-tax Act, framed by the Chief Court of Oudh, we are to give our opinion on the question of law set out in the statement of case. For reasons mentioned above and in our order under Section 19 we are of the opinion that the question should be answered in the affirmative.

11. We accordingly refer for the opinion of their Lordships of the Chief Court of Oudh at Lucknow the following question of law :—

'Whether, in the circumstances of the case, there is any material for holding that the businesses at Colonelganj (Gobardhan Das Radhey Lal), Bharwari (Babu Ram Gobardhan Das) and Bahraich (Ram Lakhan Reoti

Ram) are *carried on by the same person* (*viz.*, the firm consisting of L. Babu Ram and L. Lallu Mal) within the meaning of the second proviso to Section 2 (5) of the Excess Profits Tax Act.' "

P. D. Rastogi and *Ram Bharosey Lal*, for the assessee.

S. C. Das, for the Commissioner.

JUDGMENT.

This judgment will cover two references made by the Income-tax Appellate Tribunal on the 19th May, 1944, and the 7th September, 1944, No. 7 of 1944 and No. 9 of 1944 in this Court*. We shall also decide application No. 3 of 1944 under Section 66 (2) in the same judgment.

No. 7 arises out of the assessment of excess profits tax made for the year 7th July, 1940, to the 26th June, 1941, and No. 9 out of the assessment for the year 26th June, 1941, to the 14th-July, 1942.

The reference in each case is in identical terms,

" Whether, in the circumstances of the case, there is any material for holding that the businesses at Colonelganj (Gobardhan Das Radhey Lal), Bharwari (Babu Ram Gobardhan Das) and Bahraich (Ram Lakhan Reoti Ram) are *carried on by the same person* (*viz.*, the firm consisting of L. Babu Ram and L. Lallu Mal) within the meaning of the second proviso to Section 2 (5) of the Excess Profits Tax Act."

The facts stated in the order of reference are not challenged by learned counsel for the assessee firm. On page 1 of the printed book, line 32, we find, " It may be stated here that it was not only the case of the department, but also of the applicant firm up to 1941-42 that the three businesses belonged to the same firm of two partners, *viz.*, Babu Ram and Lallu Mal and that Colonelganj was the principal place of business and the other two places were mere branches. Returns for several years were also filed on this basis.

" It was at the 1942-43 income-tax assessment that a claim was made to the effect that a new partner, Raghunath Prasad by name, was taken in in the Bahraich concern, so that it was a separate firm, whose income should not be amalgamated with the income of the other two concerns for the purposes of assessment on the applicant firm."

The Income-tax Officer considered that Raghunath Prasad was not a *bona fide* partner and therefore assessed the excess profits tax for the year 1940-41 and for the year 1941-42 on the profits of the three businesses added together.

All these three businesses deal in cloth. In all three Babu Ram had a 12 annas share and Lallu Mal a 4 annas share. On the 31st May, 1941, according to the assessee's learned counsel these two partners Babu Ram and Lallu Mal took in another partner Raghunath Prasad. The deed of

* [The statement of case relating to Reference No. 7 of 1944 is alone included in this report. As the facts involved and the question raised in Reference No. 9 of 1944 are the same as in Reference No. 7 of 1944, the statement of case relating to Reference No. 9 of 1944 is not printed here.—Ed.]

partnership was executed on the 31st May, 1941, but it was stated in that partnership deed that the partnership had commenced from Asarh Sudi Dwij, Sambat 1997—7th July, 1940. Under this deed one anna share out of 12 annas belonging to Lala Babu Ram was given to Raghunath Prasad. He was to take the profit and bear the loss to the extent of one anna out of 16 annas. On the 1st February, 1943, the Excess Profits Tax Officer passed the orders Exhibits TA and TB. He came to the finding that Raghunath Prasad is a bogus partner and that the share of 12 annas is still held by Babu Ram. In appeal this was confirmed in Exhibit TC by the Assistant Commissioner and in Exhibit TD by the Appellate Tribunal.

It was after this that the assessee firm applied to the Tribunal to state a case. The question put to us by the Tribunal seems to contain two questions of law, only one of which however has been argued before us. The first question is whether there is any material upon which the finding that these three businesses were in fact one firm could be arrived at. This has been argued. The second is whether the word " person " in Section 2 (5), proviso 2, of the Excess Profits Tax Act includes a firm. This has not been argued by the assessee's learned counsel at all, and apparently he considers that the position is clear and agrees with the view of the Tribunal that " person " as used in that proviso does include a firm. It will be our duty to give an answer to the reference on that point also.

In our opinion the first question formulated above is a question of fact which can only be challenged if the evidence upon which the finding has been arrived at is legally insufficient to support it. We have therefore to see what that evidence is. One piece of evidence has already been given, *viz.*, that up to 1941-42 these three businesses admittedly belonged to one firm. We agree with para. 8 of the judgment of the Tribunal in reference No. 7 that it was for the assessee to prove that the three businesses were separate when admittedly they had been one and the same firm for some years previously. The evidence which the assessee gave was the partnership deed referred to above. The reasons for considering that this deed though registered is bogus are as follows.

Raghunath is a whole time employee (we are told he is a clerk) of the Free India Insurance Co., Ltd., Cawnpore, at Cawnpore. The business line is therefore foreign to him. Moreover he cannot have time to attend to the business as a working partner. Admittedly he contributed nothing to the capital of the firm and paid nothing to Babu Ram for the one anna share. Raghunath Prasad and Babu Ram are brothers-in-law so that such a fictitious arrangement could easily be made between them. The alleged change in the constitution of the firm was not notified to the Registrar of Firms as required by Section 63 (1) of the Partnership Act of 1932. There was no general change in the constitution of the firm even according to the partnership deed. The share of Lallu Mal remained unaffected. The change

moreover is alleged to have taken place nearly 11 months before the deed was executed. When the deed was executed it must have been obvious to the firm that if the three businesses were assessed together it would be liable for excess profits tax. With the exception of the allocation of profits on the closing day of the year 1941-42, there is no entry in the account books to show that Raghunath Prasad had been taken in as a partner. Moreover the assessee firm changed its case, *vide* para. 4 of the judgment of the Tribunal in Case No. 7, "It may be made clear here that in the return submitted in connection with the excess profits tax assessment income from Colonelganj and Bharwari businesses were returned by the applicant firm as belonging to the same person, *viz.*, the firm of two partners Babu Ram and Lallu Mal. But later on in connection with a separate proceeding [under Section 10 (2) of the Excess Profits Tax Act] for the same chargeable accounting period, it was claimed that even Colonelganj and Bharwari businesses did not belong to the same firm." This contention has now again been given up.

In addition to these reasons for considering that the alleged taking in of Raghunath Prasad as a partner at Bahraich is a bogus transaction the Appellate Assistant Commissioner gives some other general reasons for considering that all three businesses still belong to one firm:

"One and the same business is carried on at all three places, that is, cloth is sold partly in retail and in wholesale. Stocks for all the three shops are supplied from Cawnpore by Babu Ram, partner, who controls all these concerns. The financial arrangements are made by Babu Ram from Cawnpore for all the three concerns. Gokul Pd. who was formerly in charge of head office at Colonelganj is now in charge of Bahraich branch also. The profits of Colonelganj, Bharwari and Bahraich are also transferred to the books of Jugul Kishore Baldeo Sahai which is owned by Babu Ram through the accounts of the persons who are shown to be partners in the various branches."

There is here a mass of evidence upon which the Appellate Tribunal and the Income-tax department could come to the conclusion that all the three businesses were in fact one firm.

As we have said the question raised before the Appellate Tribunal whether the word "person" in Section 2 (5), proviso 2, includes a firm has not been argued before us, and we think it is fairly obvious that it does include a firm. In the Notes of AIYAR'S EXCESS PROFITS TAX ACT (4th Edition) p. 18, we find,

"'person' is defined in Section 2 (17) as including a Hindu undivided family, and in the General Clauses Act, 1897, which applies to all Acts, as including any company, or association or body of individuals, whether incorporated or not. The expression thus covers (*i*) individuals, (*ii*) companies, (*iii*) firms and other associations or body of individuals, and (*iv*) Hindu undivided families."

We see no reason to differ from this statement of the law.

We therefore agree with the opinion of the Tribunal that the question formulated must be answered in the affirmative and that there is material for holding that the three businesses mentioned in the reference are carried on by one and the same person, *viz.*, the firm consisting of L. Babu Ram and L. Lallu Mal.

Coming to the Application No. 3 of 1944 we find that the three questions in respect of which the assessee wishes us to order a reference to be made are :—

(*a*) Whether the provisions of Section 10 (2) applied to the facts of the case;

(*b*) Whether the imposition of a penalty of Rs. 4,000 under Section 10 (2), Excess Profits Tax Act, was legally just; and

(*c*) Whether it was legally just to apply the provision of Section 10 (2) in preference to Section 10A, if both were held applicable.

Admittedly the question of law is covered by the findings in References 7 and 9 already decided in this judgment.

Section 10 (2) provides : "If the Excess Profits Tax Officer is satisfied that any person has entered into or carried out any transaction or operation by which the profits have been or would be artificially reduced, he may, with the previous approval of the Inspecting Assistant Commissioner, direct that such person shall pay, in addition to any excess profits tax for which he is or, but for such transaction or operation, would be liable, a penalty not exceeding the tax evaded or sought to be evaded."

Section 10A (1) provides : "Where the Excess Profits Tax Officer is of opinion that the main purpose for which any transaction or transactions was or were effected whether before or after the passing of the Excess Profits Tax (Second Amendment) Act, 1941, was the avoidance or reduction of liability to excess profits tax, he may, with the previous approval of the Inspecting Assistant Commissioner, make such adjustments as respects liability to excess profits tax as he considers appropriate so as to counteract the avoidance or reduction of liability to excess profits tax which would otherwise be effected by the transaction or transactions."

In the present case there is no question of a genuine transaction, the purpose of which was the avoidance or reduction of liability to excess profits tax. The transaction, *viz.*, the execution of the new deed of partnership was a bogus transaction by which the profits "have been or would be artificially reduced."

This case therefore clearly comes under Section 10 (2) and the penalty was legally imposed. We therefore reject the application.

The assessee must pay the costs of the two references and the application. We assess the counsel's fee in each of the two references at Rs. 100 and his clerk's fee at Rs. 5 and in the application at Rs. 75 and his clerk's fee at Rs. 3-12-0. *Reference answered accordingly.*

[IN THE BOMBAY HIGH COURT.]

NEW INDIA ASSURANCE CO., LTD., BOMBAY

v.

COMMISSIONER OF INCOME TAX, BOMBAY.

SIR LEONARD STONE, C. J., and CHAGLA, J. August 23, 1946.

INDIAN INCOME-TAX ACT (XI OF 1922), SEC. 10 (7), SCHEDULE, RULES 1, 2 & 3—LIFE INSURANCE COMPANY—PARTICIPATING POLICY-HOLDERS ENTITLED TO 90 PER CENT. OF LIFE FUND—COMPUTATION OF SURPLUS—INCOME-TAX RESERVE, TAX DEDUCTED AT SOURCE, AND SUMS CARRIED FORWARD TO CREDIT OF POLICY-HOLDERS—WHETHER PAID TO OR RESERVED FOR ON BEHALF OF POLICY-HOLDERS—WHETHER HALF THE AMOUNTS DEDUCTIBLE UNDER RULE 3 (*a*).

In preparing the consolidated revenue account of the assessee, a life insurance company, the actuary took into account Rs. 33,860, being the income-tax deducted at source and Rs. 1,00,770, being the reserve for income-tax and super-tax. The assessee claimed that in computing its surplus, it was entitled to deduct one half of these two amounts under rule 3 (a) of the rules framed under Section 10 (7) of the Income-tax Act on the ground that they had been paid to or reserved for or expended on behalf of policy-holders. In support of its contention the assessee relied upon a resolution and a passage in the prospectus, the effect of which was that the policy-holders of participating policies were entitled to 90 per cent. of the life fund and the remaining 10 per cent. went to the shareholders:

Held, *that inasmuch as a life insurance company pays income-tax in discharge of its own liability and not the liability of its policy-holders the income-tax deducted at source and the income-tax reserve created by the assessee were not amounts paid to or reserved for or expended on behalf of the policy-holders within the meaning of rule 3 (a).*

The assessee further claimed that one half of a sum of Rs. 14,142 which was carried forward to the credit of the policy-holders in the statement relating to the appropriation of surplus should be deducted under rule 3 (a). The counsel for the assessee stated in the High Court that the sum was ear-marked for the policy-holders and it would not be used for any other purpose:

Held, *that this sum of Rs. 14,142 must be treated as a permissible reserve for policy-holders and the assessee was entitled to the deduction of one half of it under rule 3 (a).*

Cases referred to :—

Cull *v.* Commissioners of Inland Revenue ([1940] A.C. 51; 8 I.T.R. Suppl. 1; [1939] 3 All E.R. 761; 161 L.T. 173; 55 T.L.R. 1049; 108 L.J.K.B. 879; 22 Tax Cas. 603).

Lalita *v.* Tata Iron and Steel Co., Ltd. [1940] (8 I.T.R. 337; I.L.R. 1940 Bom. 165; 187 I.C. 389; 42 Bom. L.R. 57; A.I.R. 1940 Bom. 97; I.L.R. 1940 Bom. 165).

Reference under Section 66 (1) of the Indian Income-tax Act (XI of 1922), by the Income-tax Appellate Tribunal: (Income-tax Reference No. 7 of 1944).

STATEMENT OF CASE.

"This is a reference application made by the New India Assurance Co., Ltd., asking us to refer to the High Court of Bombay two questions of law which arise from our judgment in R.A.A. No. 126-Bombay of 1942-43. The material facts relating to the two points on which reference is asked are as follows:—

2. During the relevant accounting period the company paid a sum of Rs. 33,860 on account of income-tax deducted at source and created a reserve for the payment of income-tax of Rs. 1,00,770. The assessment has been made according to the rules made under Section 10 (7) of the Act. Under rule 2 (*b*) the surplus is to be ascertained and under rule 3 certain deductions are to be allowed from the surplus. Rule 3 (*a*) provides that half of the amount paid to or reserved for or expended on behalf of the policy-holders shall be allowed as a deduction from the surplus before arriving at the assessable profits.

3. The two items in dispute were written off in the revenue account before arriving at the surplus by the actuary. Under rule 2 (*b*) such items of expenditure which are not admissible under Section 10 have to be added back. There is no objection to this add-back to the actuarial surplus, but it is contended that as these amounts have been expended on behalf of the policy-holders they should be allowed as a deduction under rule 3 (*a*). We held that this was an expense which has to be incurred by the company and it cannot be said that this amount has been spent or reserved for the policy-holders. The liability to pay the income-tax is that of the company and not of the policy-holders. The point has been dealt in detail in paragraph 5 of our judgment (Exhibit D).

4. The previous balance brought forward of the unappropriated surplus was a sum of Rs. 11,037. It is not disputed that this sum has to be deducted from the surplus under first proviso to rule 3 (*a*). The company has carried forward to the next valuation a sum of Rs. 14,142. It was contended by the learned counsel that half of this amount should be allowed to the assessee as a deduction under rule 3 (*a*). We held that as the amount has not been definitely appropriated, and is only a carry-forward, deduction should also be allowed when the amount has been actually allocated by the company. If the assessee was to be allowed half of this amount now he could claim in a subsequent valuation half of the amount when the same has actually been appropriated. The first proviso will make the point still clearer, as it only excludes the carry-forward in the first computation. We have said in our judgment that if this proviso was not restricted to the first computation there would have been some force in the arguments

of the learned counsel for the appellant. The point has been dealt by us in paragraph 7 of our judgment (Exhibit D).

5. The two following points of law arise from our judgment and we refer them to the High Court of Judicature at Bombay, under Section 66 (1) of the Indian Income-tax Act.

Questions referred.—(1) Whether the income-tax deducted at source of Rs. 33,860 and the income-tax reserve created by the company of Rs. 1,00,770 are the amounts expended or reserved for on behalf of the policy-holders within the meaning of rule 3 (*a*) of the rules made under Section 10 (7) of the Income-tax Act?

(2) Whether the assessee is entitled to a deduction under rule 3 (*a*) of half the amount of Rs. 14,142 being the unappropriated carry-forward to the subsequent valuation period?"

This reference came before Sir Leonard Stone, C. J., and Kania, J., on the 10th November, 1944, and the reference was sent back to the Tribunal to ascertain certain additional facts.

The supplementary statement of case submitted by the Appellate Tribunal was as follows:—

SUPPLEMENTARY STATEMENT OF CASE.

"As directed by their Lordships of the Bombay High Court under Section 66 (4) of the Indian Income-tax Act, we herewith re-submit the case.

2. Inasmuch as there has been a misapprehension caused in the minds of their Lordships by the use of the word 'after' we are now stating the case at a greater length.

3. The case relates to the Life Department of the New India Assurance Co., Ltd., whose profits or gains have to be computed for income-tax purposes in accordance with the rules under Section 10 (7) of the Indian Income-tax Act. Section 10 (7) lays down:—

'Notwithstanding anything to the contrary contained in Section 8, 9, 10, 12 or 18, the profits and gains of any business of insurance and the tax payable thereon shall be computed in accordance with the rules contained in the Schedule to this Act.'

4. It is common ground that the profits and gains of the life insurance business of the applicant company are to be computed under rule 2 (*b*) of the Schedule which reads as follows:—

'The profits and gains of life insurance business shall be taken to be the annual average of the surplus arrived at by adjusting the surplus or deficit disclosed by the actuarial valuation made for the last inter-valuation period ending before the year for which the assessment is to be made, so as to exclude from it any surplus or deficit included therein which was made in any earlier inter-valuation period and any expenditure other than expenditure which

may under the provisions of Section 10 of this Act be allowed for in computing the profits and gains of a business.'

5. The assessment year is 1939-40. The last actuarial valuation made for the last inter-valuation period is for the period commencing from 1st April, 1933, and ending on 31st March, 1936.

6. The actuarial valuation report relating to the above period contains the following statements which are appended to the said report.

Consolidated revenue account for the period commencing 1st April, 1933, and ending 31st March, 1936.

	RS.	A.	P.		RS.	A.	P.
Life assurance fund at the beginning of the period ...	8,67,552	15	8	Claims paid and outstanding :— By death ... Rs. 5,96,063 By maturity ... Rs. 1,450	5,97,513	0	0
Premiums ...	62,16,973	13	8	Surrenders including surrenders of bonus additions ...	41,373	12	0
Consideration for annuities granted ...	55,839	7	0	Annuities ...	10,260	0	0
Interest [less income-tax (A) Rs. 33,860-2-1] ...	3,13,363	10	1	Commission ...	11,35,083	5	8
Assignment, enforcement and other fees ...	1,961	13	0	Expenses of management ...	14,01,341	5	10
				Contribution to staff provident fund ...	38,432	8	0
				Depreciation on furniture ...	10,931	5	5
				Transferred to reserve for bad and doubtful debts ...	11,418	15	9
				Transferred to reserve for income-tax and super-tax (B)	1,00,770	7	6
				Transferred to profit and loss account ...	8,579	0	0
				Transferred to shareholders' life profit account ...	17,158	0	0
				Investment written down ...	1,252	13	1
				Life assurance fund at the end of the period ...	40,81,577	2	2
Total ...	74,55,691	11	5	Total ...	74,55,691	11	5

In this account the actuary starts with the life assurance fund at the beginning of the period. The credit side shows all the premium receipts and other incomes. The debit side contains all the payments made on account of death, maturity and other expenses. It also includes certain reserves created to meet the liabilities during the actuarial period. Thus the actuary arrives at the balance of the life assurance fund as at the end of the actuarial period. It may be noted here that on the debit side there is an item of Rs. 1,00,770 which is the amount transferred to reserve for income-tax and super-tax. On the credit side the whole of interest income has not been included but only the cash received after the deduction of income-tax at source amounting to Rs. 33,860. It would have made no difference if the whole of the item of interest was taken on the credit side and the tax deducted shown as a revenue deduction. After having ascertained the life assurance fund at the end of the valuation period the actuary prepares the valuation

balance-sheet. The relevant valuation balance-sheet as at 31st March, 1936, is reproduced below :—

Valuation balance-sheet as at 31st March, 1936.

Dr.	RS.	A.	P.	Cr.	RS.	A.	P.
To, Net liability under life assurance and annuity transactions (as per summary statement provided in the fourth schedule) ...	33,64,294	11	2	By, life assurance and annuity funds (as per balance sheet under third schedule) ...	40,81,577	2	2
,, Surplus ...	7,17,282	7	0				
Total ...	40,81,577	2	2	Total ...	40,81,577	2	2

The actuary had a total life assurance fund of Rs. 40,81,577 as at the close of the valuation period. He had to ascertain what was the liability on the various policies in force as on that date. By preparing various statements he ascertained that the total liability under this head amounted to Rs. 33,64,294, thereby leaving a surplus of Rs. 7,17,282. This amount was available to the company to be appropriated in such manner as it thought best. The actuary submitted his recommendations which are contained in page 3 of the valuation report. He recommended that the surplus be appropriated in the following manner :—

	RS.
Surplus disclosed by the valuation ...	7,17,282·4
Less—Amount of policy-holders' share brought forward from previous valuation surplus ...	11,037·0
	7,06,245·4
Add—Interim bonus paid ...	4,530·0
Total divisible surplus ...	7,10,775·4
1/10th, being shareholders' share ...	71,077·5
	6,39,697·9
Add—Amount brought forward, *viz.*, Rs. 11,037 ...	11,037·0
Total at the credit of policy-holders ...	6,50,734·9
Provisions for bonus at Rs. 15 and Rs. 11 per thousand sum assured to whole life and other classes, respectively ...	6,32,063·3
Balance ...	18,671·6
Less—Interim bonus paid ...	4,530·0
Carry forward to the credit of policy-holders	(C) 14,141·6

The total surplus was Rs. 7,17,282. In the previous valuation report a sum of Rs. 11,037 was not appropriated to the various policy-holders as such and has gone to increase the surplus arrived at in this valuation period. This item is therefore deducted in order to arrive at the surplus relating to the relevant valuation period. During this period certain interim bonus amounting to Rs. 4,530 had already been paid by the company. Therefore

that item is added back as a part of the surplus of this period. The net divisible surplus for this valuation period is arrived at Rs. 7,10,775. According to the rules of the company, 1/10th of the surplus at the time of each valuation belongs to the shareholders. This item is therefore deducted and transferred to the shareholders' account. The balance of this item amounting to Rs. 6,39,697 *plus* Rs. 11,037 brought forward from the last valuation report remained at the disposal of the company. Out of this sum, the actuary made a provision for bonus at the rate of Rs. 15 and Rs. 11 per thousand on whole life and other classes of policies, respectively. The amount calculated by the actuary for this purpose amounted to Rs. 6,32,063. This leaves a balance of Rs. 18,671. A sum of Rs. 4,530 had already been paid during the valuation period and was added back as shown above; that has to be deducted. This leaves a balance of Rs. 14,141 which is the amount of the surplus which is not allocated to any definite policies. This will be treated in similar manner as Rs. 11,037 in the subsequent valuation report. In this valuation report, Rs. 6,32,063 were reserved for the policy-holders being the provision for bonus, and Rs. 4,530 were paid as interim bonus. Half of these two items has been allowed as a deduction under rule 3 (*a*) in computing the assessable surplus under rule 2 (*b*).

7. The surplus arrived at by the actuary is not the surplus within the meaning of rule 2 (*b*), as a number of adjustments have to be made as provided under the rules before we get to the surplus, which is assessable to tax. From the above statement it would be plain that in computing the surplus the actuary only allows deductions for such items as would fall in the consolidated revenue account. Under rule 2 (*b*) we have to take the starting figure of the surplus according to the actuarial valuation. This surplus cannot possibly take into account the provision made for policy-holders. It is only in computing the surplus for the purpose of rule 2 (*b*), *i.e.*, for ascertaining the profits and gains of an insurance business for the purpose of assessment, that further deductions are allowed as provided under the rules. We must first have a surplus as ascertained by the actuary after which we compute the surplus under rule 2 (*b*) for the purpose of assessment.

8. The dispute in the present case centres round items (A), (B) and (C). The first two appear in the consolidated revenue account and the last one appears in the statement relating to the appropriation of the surplus. It is contended by the learned counsel for the appellant that all these three items are amounts paid to or reserved for the policy-holders and half of these amounts should be allowed as a deduction under rule 3 (*a*).

9. The actuary had taken into account in preparing the consolidated revenue account two items, *viz.*, Rs. 33,860 as income-tax paid, and Rs. 1,00,770 being the reserve for income-tax and super-tax. Under rule 2 (*b*) only such items are allowed as a deduction as are allowable

under Section 10 of the Income-tax Act. Both these items cannot be allowed as an expenditure under Section 10 of the Income-tax Act. The assessee company does not object to the deduction of the above two items as provided under Section 10, but it is contended that the company is entitled to the deduction of one-half of the above two items, as these amounts have been paid to or reserved for or expended on behalf of the policy-holders, as provided under rule 3 (*a*). In support of this contention the assessee company relied upon the following evidence :—

(*a*) A resolution passed at the 316th meeting of the Life Committee held on 6th February, 1937, which reads as follows :—

"That a sum of Rs. 71,077·5 being one tenth of the surplus of Rs. 7,10,775·4 at 4 per cent. valuation be transferred in three annual instalments of Rs. 23,692·5 each to the company's profit and loss accounts."

(*b*) In the prospectus issued to the public, on page 2, the profits are defined as follows :—

"A valuation of the company's assets and liabilities is made periodically by a qualified actuary and 90 per cent. of the profits, after making the necessary provisions, is apportioned among the holders of participating policies in force for the full sum assured on the date as at which the valuation is made."

(*c*) Valuation report as at 31st March, 1936, on page 3, shows that one-tenth of the divisible surplus was allocated as shareholders' share. The balance was the share of the policy-holders. It was contended by the learned counsel for the company that on the above facts it has been proved that there is a contract between the shareholders and the policy-holders and that 90 per cent. of the surplus belongs to the policy-holders. That if the above two deductions in dispute were not provided in the account books, the surplus would have increased by the same amount. Therefore, at least 90 per cent. of this amount referred to above has been paid to or reserved for or expended on behalf of the policy-holders.

10. On the other hand, the department's contention was that the liability to pay income-tax is that of the company. That the payment of income-tax is not a payment made on behalf of the policy-holders as such. That even according to the prospectus it is clear that the policy-holders are entitled to 90 per cent. of the profits, after making necessary provisions for expenditure. That, if this proposition of the assessee was to be accepted, every expenditure incurred by the company, as shown in the consolidated revenue account, could be treated as the amount spent on behalf of the policy-holders because it will go to increase the surplus if such a deduction has not been made by the actuary.

11. We agreed with the learned counsel for the department that the two amounts in dispute were neither paid to nor reserved for nor expended

on behalf of the policy-holders. The company is a separate entity in law and the liability to pay income-tax is that of the assessee company, and not that of the policy-holders.

12. The assessee company had asked us to state a case on two points. We have dealt with the first point. We think, in the light of the observations made by their Lordships, it would be better if we deal with the second point also. In the second case, the assessee claims half of Rs. 14,141 as a deduction under rule 3 (*a*). In order to understand clearly the point in issue we would again refer to the recommendations made by the actuary as regards the appropriation of the surplus. During the actuarial valuation period under reference the amount reserved for and allocated to various policies in the form of bonus amounted to Rs. 6,32,063. The interim bonus paid amounted to Rs. 4,530. Half of both these items has been allowed to the assessee company as a revenue deduction under rule 3 (*a*) in computing the assessable surplus under rule 2 (*b*). It will be noticed that the carry forward of the balance to the subsequent valuation period amounting in all to Rs. 14,141 includes the opening balance brought forward from the preceding year, amounting to Rs. 11,037. Suppose the assessee company had already claimed half of Rs. 11,037 as a deduction under rule 3 (*a*) in the previous valuation period the company would get a double deduction on this amount if half of Rs. 14,141 was again allowed in this valuation period.

13. This item of Rs. 14,141 is really composed of the unappropriated surplus brought forward from the preceding valuation report and the unappropriated surplus of the relevant valuation period. The surplus as disclosed by the valuation balance-sheet was Rs. 7,17,282. This included unappropriated surplus brought forward from the previous valuation report, amounting to Rs. 11,037. So that the surplus relating to the valuation period under reference was Rs. 7,06,245, neglecting the small item of Rs. 4,000 and odd which had been paid, as it has to be added back and deducted again. This was appropriated in the following manner :—

Shareholders' share	Rs. 71,077·5
Provisions for bonus on policies	Rs. 6,32,063·3

Thus leaving a balance of Rs. 3,104 [Rs. 7,06,245—(Rs. 71,077·5 plus Rs. 6,32,063·3)] being the unappropriated surplus out of the surplus relating to the valuation period. We held that the company could only claim the deduction under rule 3 (*a*) of such items as were paid to or reserved for the policy-holders. This item, in our opinion, was neither paid to nor reserved for any of the policy-holders.

14. Perhaps, it would have been proper if we had dismissed the application for reference as the questions involved were of fact. But as the case is already before their Lordships we will submit the same questions as we

had framed in the original statement of the case for their Lordships' opinion."

Sir Jamshedji Kanga, for the assessee.
Motilal Setalvad, for the Commissioner.

JUDGMENT.

STONE, C.J.—This matter came before my learned brother Sir Harilal Kania and myself on the 10th of November, 1944, when we sent the reference back to the Tribunal to ascertain certain additional and necessary facts. We then pointed out that the Tribunal had made an incorrect approach to rules 2 (*b*) and 3 (*a*) of the Schedule to the Income-tax Act to which I will presently refer. The point which arises when analysed resolves itself into an extremely narrow one. By Section 10 (7) of the Income-tax Act, it is provided that notwithstanding anything to the contrary contained in Sections 8, 9, 10, 12 or 18, the profits and gains of any business of insurance and the tax payable thereon shall be computed in accordance with the rules contained in the Schedule to the Act. Turning to the Schedule it will be found that rule 1 provides :—

" In the case of any person who carries on, or at any time in the preceding year carried on, life insurance business, the profits and gains of such person from that business shall be computed separately from his income, profits or gains from any other business."

Rule 2 provides :—

" The profits and gains of life insurance business shall be taken to be either—"

Then two alternatives are given, and it is the greater which is to be taken. In this case it is the second alternative, *viz.*, that which is lettered (*b*) which is relevant, It provides : " the annual average of the surplus arrived at by adjusting the surplus or deficit disclosed by the actuarial valuation made for the last inter-valuation period ending before the year for which the assessment is to be made, so as to exclude from it any surplus or deficit included therein which was made in any earlier inter-valuation period and any expenditure other than expenditure which may under the provisions of Section 10 of this Act be allowed for in computing the profits and gains of a business."

But it is to rule 3 to which importance is attached in this case :—

" In computing the surplus for the purpose of rule 2,—

(*a*) one-half of the amounts paid to or reserved for or expended on behalf of policy-holders shall be allowed as a deduction."

It is under that sub-rule that the three sums with which we are concerned are said to fall.

In remitting their supplemental case, the Tribunal has not raised any fresh question. Therefore, the questions which we have to consider are those which are to be found in the original case which are :—

(1) Whether income-tax deducted at source of Rs. 33,860 and the income-tax reserve created by the company of Rs. 1,00,770 are the amounts expended or reserved for or on behalf of the policy-holders within the meaning of rule 3 (*a*) of the rules made under Section 10 (7) of the Income-tax Act?

(2) Whether the assessee is entitled to a deduction under rule 3 (*a*) of half the amount of Rs. 14,142 being the unappropriated carry-forward to the subsequent valuation period?

On behalf of the assessee, the insurance company, Sir Jamshedji Kanga has submitted that any amount which the company expends out of its life fund is an expenditure on behalf of its policy-holders, because they are virtually the owners of the fund. With regard to that submission the following further material is to be found in the supplemental case, paragraph 9 :—

"The actuary had taken into account in preparing the consolidated revenue account two items, *viz.*, Rs. 33,860 as income-tax paid, and Rs. 1,00,770 being the reserve for income-tax and super-tax. Under rule 2 (*b*) only such items are allowed as a deduction as are allowable under Section 10 of the Income-tax Act. Both these items cannot be allowed as an expenditure under Section 10 of the Income-tax Act. The assessee company does not object to the deduction of the above two items as provided under Section 10, but it is contended that the company is entitled to the deduction of one-half of the above two items, as these amounts have been paid to or reserved for or expended on behalf of the policy-holders, as provided under rule 3 (*a*). In support of this contention the assessee company relied upon the following evidence :—"

Then are set out, first of all, a resolution and a quotation from the prospectus, the effect of which is to show that the policy-holders of participating policies are entitled to 90 per cent. of the life fund, whereas the remaining 10 per cent. goes to the shareholders.

On the other hand, Mr. Setalvad on behalf of the Income-tax authorities submits that income-tax paid by the insurance company is paid on behalf of itself and no one else, and in support of that proposition the case of *Lalita* v. *Tata Iron and Steel Co., Ltd.* [1], is relied upon, as is also a case in the House of Lords: *Cull* v. *Commissioners of Inland Revenue* [2], in which Lord Atkin at page 56 said that the company pays income-tax in discharge of its own liability and not as agents for its shareholders. Be it observed that policy-holders are still further removed than shareholders in

(1) [1940] 8 I.T.R. 337; 42 Bom. L.R. 57.

(2) [1940] A.C. 51; 8 I.T.R. Suppl. 1.

their relationship with the company and that their rights rest in the contracts provided by their policies. In my judgment this argument is well founded. So far as the sum of Rs. 33,860 is concerned, it represents the amount deducted at source from the interest payable to the company on its invested funds and it is, therefore, deducted in part discharge of the liability of the company to pay its own taxes. It is to be observed that there is no such provision, as Section 49B of the Income-tax Act, which could apply to policy-holders. That section was enacted to give special rights to shareholders in respect of income-tax paid by the company of which they are members. I cannot see how it can be said that this Rs. 33,860 has been paid on behalf of the policy-holders, especially is this so when there is no liability whatever on them to pay this amount.

With regard to Rs. 1,00,770, this is a provision which under the Insurance Act must be made by the insurance company, and it is a liability which must be provided for before the surplus can be shown in the revenue accounts of the life department. In the company's annual revenue accounts of the life department no figures in respect of income-tax are shown except a single separate figure for each of the three years ; the total of these figures for the 3 years is the sum of Rs. 1,00,770. In each year there is in fact a separate amount reserved, and these annual reservations are no doubt adjusted when it is discovered whether the reserve of the preceding year was more or less than the actual amount which had to be paid to discharge the income-tax. In my opinion this sum of Rs. 1,00,770 cannot be said to be reserved for or expended on behalf of the policy-holders any more than the sum of Rs. 33,860. Even if it could, the deduction would have to be brought back again under the proviso to rule 3 (*a*), whereby it is laid down that if any amount so reserved for policy-holders ceases to be so reserved, and is not paid to or expended on behalf of policy-holders one-half of such amount, if it has been previously allowed as a deduction, shall be treated as part of the surplus for the period in which the said amount ceased to be so reserved. But in my opinion that provision never becomes operative, because neither the Rs. 33,860 nor the Rs. 1,00,770 is a permissible deduction under rule 3 (*a*).

That leaves the second question with regard to a sum of Rs. 14,141, which is to be found in the accounts described as a carry-forward to the credit of policy-holders. Sir Jamshedji Kanga on behalf of the insurance company has stated in this Court that the Rs. 14,141 is not only carried forward to the credit of the policy-holders, but is ear-marked for the policy-holders and that it will be used for no other purpose. On that statement by counsel being made Mr. Setalvad on behalf of the Commissioner does not press the matter further, and this sum must be treated as a permissible reserve for policy-holders within the terms of rule 3 (*a*).

The answer to the questions, therefore, which I propose is that question No. 1 be answered in the negative and question No. 2 in the affirmative.

CHAGLA, J.—I agree.

The first contention raised by Mr. Setalvad is that the question referred to us, "whether the income-tax deducted at source of Rs. 33,860 and the income-tax reserve created by the company of Rs. 1,00,770 are the amounts expended or reserved for on behalf of the policy-holders within the meaning of rule 3 (*a*) of the rules made under Section 10 (7) of the Income-tax Act," is a question of fact, and Mr. Setalvad says that inasmuch as the Tribunal has come to the conclusion that these sums are not reserved for nor expended on behalf of the policy-holders, we cannot go behind that finding of fact. I do not accept that contention of Mr. Setalvad. The question referred to us is a question of law. We have been asked to consider whether the conclusion arrived at by the Tribunal from admitted or proved facts is a conclusion justified in law, whether the conclusion is justified on a true construction of rule 3 (*a*) of the rules framed under the Income-tax Act.

Now, the question of the applicability of a section or the construction of a section is always a question of law. Mr. Setalvad has relied, and from his point of view rightly relied, on an expression used by Mr. Justice Kania, when he referred this matter back to the Tribunal for a further statement of facts, the expression being that the question whether the amount in question was paid to or reserved for or was expended on behalf of the policy-holders is a question of fact. I do not think it is fair to the learned Judge to wrench that expression from its context. When one looks at the context, it is clear, what the learned Judge means, and really, if the question referred to us was a question of fact, I fail to see the necessity for referring it back to the Tribunal for a further and better statement of the case.

Now the scheme of rules 2 and 3 framed under Section 10 (7) of the Income-tax Act to my mind is perfectly clear. The profits and gains of a life insurance business are to be assessed under rule 2 (*b*) on the surplus arrived at on an actuarial valuation subject to certain deductions and additions. First the actual surplus arrived at by the actuary is to be taken as the basis. Then under rule 2 (*b*) there is to be excluded from that surplus two amounts, first any surplus or deficit which is included in it which was made in any earlier inter-valuation period and does not belong to the valuation period under consideration and the second amount to be excluded is all such expenditure as is not permissible under Section 10 of the Income-tax Act. Then under rule 3 certain deductions are allowed and the most important deduction and the one which we have got to consider for the purpose of this reference is the deduction permitted under rule 3 (*a*) which

is one-half of the amounts paid to or reserved for or expended on behalf of policy-holders. Now under Section 13 of the Insurance Act an actuarial report and abstract have got to be prepared as part of the statutory obligation of a life insurance company and in Schedule IV to that Act a form is given, Form G, which lays down the manner in which a consolidated revenue account has to be prepared. It is important to note that in this form one of the items of expenditure shown on the debit side is taxes paid in United Kingdom, British India, Dominion and foreign countries and on the credit side is shown interest, dividends and rents but less income-tax thereon, which undoubtedly means income-tax deducted at the source. Therefore, in order to arrive at a proper actuarial surplus, the Insurance Act requires that certain expenses must be first deducted and among those expenses are payments of income-tax. Therefore, before the surplus in this case of Rs. 7,17,282-7-0 was arrived at by an actuarial calculation, the sum of Rs. 1,00,770-7-6 was debited as transferred to reserve for income-tax and super-tax and also the sum of Rs. 33,860 was deducted from the interest earned as income-tax deducted at the source. What the actuary was doing was what he was bound to do under the law, *viz.*, to make these deductions before he certified that the surplus was Rs. 7,17,282-7-0.

Now I fail to understand, with great respect to Sir Jamshedji Kanga, the argument that if these two deductions were not provided for in the account books, the surplus would have been increased by the same amount. Whether entries were made to this effect in the account books or not, I fail to see how the surplus could have been increased which could have been divisible among the shareholders. The contract between the company and the shareholders, which is referred to in the supplementary statement, is that 90 per cent. of the profits, after making the necessary provisions, is to be apportioned among the holders of participating policies and it cannot possibly be urged that one of the necessary provisions is not the payment of income-tax. Therefore, and after all, the only relationship between the company and its policy-holders is a contractual one, under the contract a policy-holder can only claim to be entitled to 90 per cent. of the profits after proper expenditure has been incurred, and one of those items of expenditure would be the payment of income-tax.

The real question we have to consider is whether these two amounts have been reserved for or expended on behalf of the policy-holders. Sir Jamshedji Kanga has rightly conceded that there is no difference in principle between these two amounts; the sum of Rs. 33,860-2-1 has been actually expended, the sum of Rs. 1,00,770-7-6 is not expended but it is kept in reserve to meet a liability similar to the liability for which Rs. 33,860-2-1 was expended.

It is not disputed and it cannot be disputed that the assessee in this case is the company. The liability to pay the tax is on the company. There

is no liability to pay the tax on the policy-holders, and the amount of Rs. 33,860-2-1 was paid by the company not on anyone else's behalf but on its own behalf in order to discharge a liability which in law it has to discharge for paying income-tax. Similarly the sum of Rs. 1,00,770-7-6 is reserved by the company to meet a liability which again is in law its own liability and not the liability of the policy-holders. In face of that I find it very difficult to appreciate Sir Jamshedji Kanga's argument that these two amounts were either expended or reserved on behalf of the policy-holders.

With regard to the sum of Rs. 14,142, I really fail to understand how the Tribunal in face of the appropriation account came to the conclusion that this was the unappropriated surplus. In the total which is placed to the credit of the policy-holders, *viz.*, Rs. 6,50,734 the sum of Rs. 14,142 is included. Instead of paying out the whole of this amount, what the appropriation account does is, it pays out or makes provision for the payment of Rs. 6,32,063 to the policy-holders, provides for Rs. 4,530, which is the interim bonus already paid, and carries forward the balance of Rs. 14,141 to the credit of the policy-holders. It is already appropriated, remains appropriated and is carried forward as appropriated to the credit of the policy-holders. To remove all ambiguity Sir Jamshedji Kanga has made a statement, as referred to by the learned Chief Justice, on behalf of the company that this sum is ear-marked for the policy-holders and will not be utilised for any other purpose.

Under the circumstances I agree with the learned Chief Justice that the question referred to us should be answered in the manner he has suggested.

P.C.—We think that in the circumstances each party should pay his own costs.

Reference answered accordingly.

[IN THE BOMBAY HIGH COURT.]

VITHALDAS THAKORDAS AND COMPANY

v.

COMMISSIONER OF INCOME-TAX, BOMBAY.

SIR LEONARD STONE, C. J., and CHAGLA, J.

October 8, 1946.

INDIAN INCOME-TAX ACT (XI OF 1922), SEC. 10 (2) (*xii*)—BUSINESS EXPENDITURE—PARTNERSHIP—PAYMENT TO THIRD PARTY OF A SHARE OF NET PROFITS FOR USE OF GOODWILL—WHETHER APPROPRIATION OF PROFITS—WHETHER REVENUE EXPENDITURE—WHETHER WHOLLY AND EXCLUSIVELY INCURRED FOR PURPOSES OF BUSINESS.

After the death of V, who had during his lifetime carried on in his own name a bullion business, the assessees, a firm of partners, entered into an arrangement with the widow of V for the use of V's name for their bullion business. Under the arrangement, in consideration of the widow having agreed to allow the partners to use the name of V for the purpose of the partnership business the partners agreed to pay to her out of the net profits of the business in the first instance an amount equivalent to two annas in the rupee of the net profits. The partners also agreed that neither she nor the estate of V would be liable for the debts or losses of the partnership and that she would not be deemed a partner in the business. The partnership deed provided that after payment of the aforesaid amount to the widow, the balance of the net profits was to be divided between the partners in certain proportions. No term was fixed for the duration of the use of the goodwill. In the accounting year the assessees made a net profit of Rs. 40,470 and the widow was paid Rs. 5,059, being her share in the profits :

Held, *that the sum of Rs. 5,059 paid to the widow was not an appropriation of the profits of the partnership after they had been ascertained, that the agreement was not in the nature of a joint venture or a quasi partnership, and that the payment was a revenue expenditure wholly and exclusively incurred for the purposes of the business, and was admissible for deduction under Section 10 (2) (xii) of the Indian Income-tax Act.*

Cases referred to :—

British Sugar Manufacturers, Ltd. *v.* Harris ([1938] 2 K.B. 220 ; 107 L.J.K.B. 472 ; 21 Tax Cas. 528 ; 159 L.T. 365; 82 S.J. 75; 1938, 1 All E.R. 428; 7 I.T.R. 101).

Commissioner of Income-tax, Bombay *v.* C. Macdonald & Co. [1935] (3 I.T.R. 459; 7 I.T.C. 466; 37 Bom. L.R. 126 ; A.I.R. 1935 Bom. 197 ; 156 I.C. 274).

Commissioner of Income-tax, Bombay Presidency *v.* Tata Sons Ltd. [1939] (7 I.T.R. 195 ; 183 I.C. 780 ; 41 Bom. L.R. 362 ; 1939 Bom. 283).

Indian Radio and Cable Communications Company Ltd. *v.* Commissioner of Income-tax Bombay Presidency and Aden [1937] (5 I.T.R. 270 ; 168 I.C. 769 ; 41 C.W.N. 869 ; I.L.R. 1937 Bom. 591 ; 46 L.W. 72 ; 39 Bom. L.R. 1025 ; A.I.R. 1937 P.C. 189).

Ogden *v.* Medway Cinemas Ltd. [1934] (18 Tax Cas. 691).

Pondicherry Railway Co. *v.* Commissioner of Income-tax [1931] (I.L.R. 54 Mad. 691 ; 58 I.A. 239 ; 61 M.L.J. 251 ; 33 Bom. L.R. 1263 ; 35 C.W.N. 895 ; 132 I.C. 619 ; A.I.R. 1931 P.C. 165 ; 5 I.T.C. 363).

Tata Hydro-Electric Agencies Ltd. *v.* Commissioner of Income-tax, Bombay [1937] (5 I.T.R. 202 ; 64 I.A. 215 ; I.L.R. 1937 Bom. 388 ; 41 C.W.N. 774 ; 39 Bom. L.R. 775 ; 46 L.W. 60 ; 168 I.C. 173 ; A.I.R. 1937 P.C. 139 ; 1937, 2 M.L.J. 763).

Union Cold Storage Co. Ltd. *v.* Adamson [1930-31] (144 L.T. 140 ; 146 L.T. 172 ; 16 Tax Cas. 293).

Case referred under Section 66 (1) of the Indian Income-tax Act (XI of 1922), as amended by Section 92 of the Income-tax (Amendment) Act, 1939 (VII of 1939) : Income-tax Reference No. 13 of 1944.

STATEMENT OF CASE.

" This is a reference under Section 66 (1) of the Indian Income-tax Act, 1939, at the instance of the assessee firm of Messrs. Vithaldas Thakordas & Co. The application in this connection is marked Exhibit A.

The assessee asks us to refer certain questions of law arising out of our judgment in his Regular Assessment Appeal No. 33, Bombay, 1943-44, for their Lordships' opinion. The Commissioner of Income-tax, Bombay, Sind and Baluchistan, has filed a written answer which is Exhibit B.

2. The assessee's appeal to the Income-tax Appellate Tribunal arose out of his assessment to income-tax for the charge year 1942-43. The material undisputed facts are stated in paragraphs 2, 3, and 4 of our judgment. For the purpose of this reference they may be briefly recapitulated. One Vithaldas Thakordas was carrying on a bullion business in Bombay under the style of Messrs. Vithaldas Thakordas & Co. It was his proprietary concern. He died in 1930, leaving a widow Mrs. Tarabai. After his death, the business was taken over by four persons, Messrs. Jamnadas, Maganlal, Sakarchand and Ratilal who continued it in partnership. The instrument of partnership in this connection is dated July 3, 1934. With the consent of Mrs. Tarabai they adopted the trade name of her late husband, and in consideration agreed to make her an annual payment equivalent to a two-anna share of the net profits without her being liable for any losses of the firm. This provision is contained in clause 4 of the partnership deed. Sometime later, Sakarchand left the firm and since then the business is being continued by the remaining three in partnership constituted by a fresh deed dated January 25, 1939. Clause 6 of this deed reiterates the agreement made in the earlier deed in connection with the annual payment to Mrs. Tarabai. In the year of account material to the present assessment the assessee firm paid the lady a sum of Rs. 5,059 equivalent to a two-anna share in the net profits of the firm, and claimed it for deduction as an item of revenue expenditure under Section 10 (2) (xii) of the Indian Income-tax (Amendment) Act, 1939.

3. Both the Income-tax Officer and the Appellate Assistant Commissioner rejected the claim. Their orders are, respectively, Exhibits C and D. The assessee took an appeal R.A.A. No. 33, Bombay, 1943-44, to the Tribunal and we upheld the view of the Appellate Assistant Commissioner and dismissed the appeal. A copy of our judgment is Exhibit E.

4. On a consideration of the facts and the material clause in the deed of partnership a copy of which is Exhibit F, we held in the first instance that the payment to Mrs. Tarabai was not an expense but was really application or appropriation of the assessee's profits. We also held that even if the payment amounted to expenditure it was of a capital nature. Reasons for these conclusions have been recorded in paragraphs 5 to 8 of our judgment.

5. The assessee has proposed three questions for submission to their Lordships while the Commissioner has formulated only one. We think that the following two questions of law may be referred for their Lordships' opinion :—

Questions referred :—(1) Whether in the circumstances of the case the payment of Rs. 5,059 made by the assessee firm to Mrs. Tarabai widow of Vithaldas Thakordas was rightly held to be an appropriation of profits?

(2) If the sum paid to Mrs. Tarabai was an item of expenditure, whether in the circumstances it was an item of revenue expenditure, and admissible for deduction under Section 10 (2) (xii) of the Indian Income-tax Act, 1939?"

This reference was sent back to the Tribunal by the Court on October 11, 1944, to ascertain certain additional facts.

The supplementary statement of case submitted by the Tribunal was as follows:—

SUPPLEMENTARY STATEMENT OF CASE.

"In accordance with the direction in their Lordships' order dated, October 11, 1944, we are submitting the following supplementary statement of the case in the above reference.

2. Before doing so, and for the purpose of a connected narration, we shall briefly refer to the facts stated in the case submitted to their Lordships earlier. The assessees who are a firm which, in 1934, consisted of four partners and, since 1939, consists of three, are carrying on bullion business in Bombay in the trade name of Messrs. Vithaldas Thakordas & Co. It was the name of a similar business that one Vithaldas Thakordas was carrying on till his death in 1930. Thereafter his widow Bai Tarabai became the owner of the goodwill, and the assessees are using it with the lady's consent in consideration of an annual payment of a two-anna share out of the net profits of the business. The instruments of partnership of 1934 and 1939 contain express clauses in this respect. In the year of account material to their present assessment, the assessees paid the lady a sum of Rs. 5,059 equivalent to a two-anna share of the net profits of the business and claimed the amount for deduction as a revenue expense under Section 10 (2) (xii) of the Indian Income-tax Act. The Income-tax authorities disallowed the payment and we sustained their orders mainly on the ground that the payment in question was an appropriation of the profits. Alternatively, we held that the expenditure was of capital nature.

3. Their Lordships observed that the agreements contained in the partnership instruments were between the partners *inter se*, and that it was necessary to ascertain the terms of the arrangement between Bai Tarabai and the assessee firm in connection with the use of the trade name in order to determine the nature of the payment, that is to say, whether the lady had sold the goodwill to the assessees or only granted a licence for its use. Accordingly, they sent the matter back to enable us to state further facts on these points.

4. The evidence on the facts that their Lordships have required us to state has been now produced. It consists of four documents. It appears

that the firm really started business in bullion in the trade name of Messrs Vithaldas Thakordas & Co., in July 1931. It then consisted of five partners. The first of the documents just referred to is an agreement dated 1st July, 1931, between Bai Tarabai and the five partners, whereby she agreed to their using her husband's trade name for a period of one year and four months in consideration of an annual payment of two annas share out of the net profits with a right to terminate the user at the end of the period. The agreement, however, was renewed from time to time till July, 1934, when one of the partners died and the firm was reconstituted of the remaining four partners. The second document is an agreement dated 3rd July, 1934, between the lady and the four partners and is in similar terms. The period for which the use of the trade name was granted was one year and four months, in the first instance. The third document is a counterpart of the second executed by the lady on the same day. The period of user appears to have been extended till December, 1938, when one of the four partners died, and the firm came to be again reconstituted of the present three partners by an instrument dated January 25, 1939. This time the arrangement was renewed, but there was no formal agreement. And the fourth document relied on in this connection is a letter dated January 30, 1939, written by the partners to Bai Tarabai. Paragraph 1 of this letter is as follows :—

'We beg to note that an agreement has been arrived at between us and you that in consideration of your having agreed to allow us the use of the name of Vithaldas Thakordas and to carry on our business in the firm name of Vithaldas Thakordas & Co., we shall out of the net profits of the business pay to you in the first instance an amount equivalent to 2 annas in the rupee of such net profits.' The rest of the letter is not material.

5. From the above extract it will be clear that there is no stipulation as to the period for which the assessees may use the trade name; nor is there any stipulation as to revocation of the use by the lady. The substance of the arrangement contained in these several documents is repeated in a joint affidavit of the lady and two out of the three partners dated 18th April, 1945. It is stated therein that the lady has not sold the goodwill to the assessee firm but merely allowed them the licence to use the goodwill in consideration of a payment of two annas share in the net profits of the firm. At the desire of the petitioner's solicitors we are including all these documents in the case as annexures G, H, J, K, and L respectively.

6. We find upon this evidence that Bai Tarabai has not sold the goodwill of her late husband to the assessee firm but has only permitted them to use it and that since 1939 the use is not subject to any stipulation as to period. The agreements of 1931 and 1934 as well as the letter of 1939 are silent as to whether the lady is to be paid anything for the use of the goodwill in the event of the firm making a loss in any year. Presumably, no

such payment is to be made to her in the event of the firm's business resulting in loss in a year. Further, since 1939, the lady has not reserved to herself the power of revocation of the use at will or otherwise.

7. In this connection, we respectfully desire to state that, in appeal before us, it was not the Department's case that the lady had sold the goodwill to the assessees. On the contrary, it was common ground between the two sides that she had permitted the assessees to use the trade name. In paras. 3 and 8 of our appellate judgment we have spoken of the payment made to the lady as consideration for the use of the trade name. At the hearing of the assessees' appeal we were not informed of the nature and terms of the arrangement between the lady and the assessees and both sides only relied on the clauses of the partnership instruments in support of their respective cases. We considered the nature of the payment to the lady from the point of view of the assessees being permitted to use the trade name. But that did not make any difference to our conclusion having regard to the express agreements that the annual payment was to be made out of the net profits."

Sir Jamshedji B. Kanga, for the assessees.

M. C. Setalvad, for the Commissioner.

JUDGMENT.

STONE, C. J.—The judgment about to be delivered by my learned brother is the judgment of the Court.

CHAGLA, J.—This is a reference under Section 66 (1) of the Indian Income-tax Act and is with regard to the assessment for income-tax purposes of Messrs. Vithaldas Thakordas & Co., a firm, in respect of the assessment year 1942-43, the relevant accounting period being the 1st November, 1940, to the 20th October, 1941.

The point which we have to determine concerns the sum of Rs. 5,059 and is a short one, though not one which is free from difficulty. As referred to us by the Tribunal, the questions asked are :—

(1) Whether in the circumstances of the case the payment of Rs. 5,059 made by the assessee firm to Mrs. Tarabai widow of Vithaldas Thakordas was rightly held to be an appropriation of profits?

(2) If the sum paid to Mrs. Tarabai was an item of expenditure, whether in the circumstances it was an item of revenue expenditure, and admissible for deduction under Section 10 (2) (xii) of the Indian Income-tax Act, 1939 ?

On the 1st of November, 1930, Mr. Vithaldas Thakordas died, leaving his widow, Bai Tarabai, him surviving. He had, during his lifetime, carried on in his own name a bullion business of which he was the proprietor, and upon his death under arrangements made by Bai Tarabai in the first instance with five persons and subsequently with four of them the name "Vithaldas Thakordas" was used by these persons in carrying

on their own business in partnership. One of the four persons died and on the 25th of January, 1939, by a partnership deed of that date, the firm was reconstituted by the three survivors and a new arrangement was entered into by the new partnership with Bai Tarabai for the use of the name "Vithaldas Thakordas." Whether the consideration, being the sum of Rs. 5,059 paid by the new partnership to Bai Tarabai for the use of the name, is a deduction within the meaning of Section 10 (2) (xii) of the Act must depend not only upon the construction of that sub-section but upon the nature of the arrangements entered into by the partners. However, when this reference first came before this Court, the arrangements, which it now appears were evidenced by a written document, were not included in the case referred to us. Accordingly on the 11th of October, 1944, the reference was remitted back to the Tribunal, and our learned brother Kania in delivering the judgment of this Court said:—

"In the absence of the necessary findings about the nature and the terms of arrangement between Mrs. Tarabai and the assessee firm we are unable to consider the questions referred to us. Under the powers vested in this Court under Section 66 (4) of the Act we therefore refer the matter back to the Tribunal to enable them to state to the Court further facts in respect of the nature and terms of arrangement between Mrs. Tarabai and the assessee firm in connection with the use of the name of Messrs. Vithaldas Thakordas & Co. by the assessee firm in respect of their bullion business in the year of account."

Section 10 (2) of the Act provides that profits and gains of any business, profession or vocation shall be computed after making the allowances mentioned in the sub-paragraphs to that sub-section and it is with sub-paragraph (xii) with which we are concerned. It is as follows:—

"any expenditure (not being in the nature of capital expenditure or personal expenses of the assessee) laid out or expended wholly and exclusively for the purpose of such business, profession or vocation."

So in order to come within sub-paragraph (xii) the sum in question must be an expenditure, which is not in the nature of a capital expenditure, and it must be an expenditure "wholly and exclusively for the purpose" of the business.

In this case it is submitted by Mr. Setalvad on behalf of the Commissioner that the Rs. 5,059 is not an expenditure at all, because it is said the payment represents a share of profits and it is also submitted that in any event it is a capital expenditure.

The Tribunal has now submitted its supplemental case and has annexed to it the letter of agreement dated the 30th of January, 1939, addressed to Bai Tarabai and signed by the three partners. The partnership deed of the 25th January, 1939, is to be found annexed to the original case. By that document the three persons parties thereto mutually agreed that they

should become partners on the terms thereinafter contained, and after stating the nature of their business the deed provides that the partnership should commence from the 27th January, 1939, and that the firm shall be "Vithaldas Thakordas & Co." Paragraphs 6 and 7 are as follows :—

"6. In consideration of Bai Tarabai, widow of Vithaldas Thakordas, having agreed to allow the partnership to use the name of Vithaldas Thakordas for the purpose of the partnership, the partnership shall out of the net profits of the business pay to her the said Bai Tarabai in the first instance an amount equivalent to two annas in the rupee of the net profits. In case the partnership suffers loss the said Bai Tarabai shall not be liable for any part thereof.

7. After payment of the amount as aforesaid to Bai Tarabai out of the net profits the balance of the net profit shall be divided between the partners in the following proportions :—

(1) The said Jamnadas Monji shall be entitled to 0-7-0.

(2) The said Maganlal Lalji shall be entitled to 0-3-9 ; and

(3) The said Ratilal Chhabildas shall be entitled to 0-3-3 in the unit of 14 annas ; and they shall in the like proportion bear all the losses.

8. Nothing in this agreement shall constitute the said Bai Tarabai a partner in the firm of Messrs. Vithaldas Thakordas & Co."

The letter of the 30th January, 1939, addressed to Bai Tarabai is headed "Re : Partnership agreement between," and then follow the names of the three partners. The rest of the document is in these terms :—

"We beg to note that an agreement has been arrived at between us and you that in consideration of your having agreed to allow us the use of the name of Vithaldas Thakordas and to carry on our business in the firm name of Vithaldas Thakordas & Co., we shall out of the net profits of the business pay to you in the first instance an amount equivalent to two annas in the rupee of such net profits.

In case the partnership suffers any loss you will not be liable for any part thereof.

By reason of your having allowed us the use of the name of Vithaldas Thakordas and/or by payment of the share in the net profits as aforesaid you will not be deemed to be a partner in the said firm of Messrs. Vithaldas Thakordas & Co., and neither you nor your heirs executors administrators or assigns or the estate of the said Vithaldas Thakordas will be in any way liable for the debts or losses of the said partnership.

We hereby further agree to keep you and the estate and effects of Vithaldas Thakordas deceased harmless and indemnified against all loss or damage that you or the estate of Vithaldas Thakordas may suffer by reason of your having allowed us the use of the name of Vithaldas Thakordas as aforesaid."

It is clear on these two material documents, the partnership deed and the letter written by the three partners to Bai Tarabai, that Bai Tarabai

allowed the use of the goodwill to the partnership firm for a consideration of her receiving two annas in the rupee of the "net profits" of the firm. No term is fixed for the duration of the use of the goodwill and apparently the agreement is terminable at will.

In the accounting year the firm made a net profit of Rs. 40,470 and Bai Tarabai's share in these profits came to Rs. 5,059. The question which arises for our determination is whether this amount is an expenditure not being in the nature of a capital expenditure which has been expended wholly and exclusively for the purpose of the partnership business.

In our opinion it is clear that the expenditure is not in the nature of a capital expenditure. By paying a two annas share in the net profit the partnership did not acquire any asset. It paid a fee or rent for the use of the goodwill and that can only be a revenue expenditure. If the partnership had acquired the goodwill by paying a lump sum, undoubtedly that would have been a capital expenditure; or even if instead of paying a lump sum it had paid the amount fixed for the goodwill by certain instalments, each instalment would have been in the nature of a capital expenditure. But in this case, as the partnership did not acquire anything in the nature of a permanent asset, the payment to Bai Tarabai is not a capital but a revenue expenditure. The case of *Ogden* v. *Medway Cinemas, Ltd.*[1] is very similar to the one before us. There the assessee obtained the lease of a hall to be used as a cinema theatre, and by a supplemental deed executed on the same day the assessee was also permitted the use of the goodwill for an annual payment of £ 500. Mr. Justice Finlay held that the payment of £ 500 was not the payment of the capital sum but was a necessary revenue expense of the assessee.

The other and the more important question is whether the amount paid to Bai Tarabai is the appropriation of the profits of the partnership after they have been ascertained? Or is it a permissible deduction which has got to be made before the profits of the firm are ascertained? Under Section 10, sub-section (1), of the Act the tax is made payable by the assessee in respect of the profits or gains of his business; and under sub-section (2) such profits or gains are to be computed after the allowances set out in that sub-section have been made; and one of such allowances is the expenditure wholly and exclusively for the purpose of the business mentioned in sub-clause (xii) of Section 10 (2) of the Act. Once the permissible deductions are made out of the profits, the profits attract the tax and it is no concern of the revenue authorities how these profits are appropriated or distributed or what the destination of the profits might be. Therefore the narrow question that we have got to consider is whether the assessees are entitled to deduct the payment made to Bai Tarabai as reasonable expenditure before the profits of the firm become liable to tax or is the payment

(1) (1934) 18 Tax Cas. 691.

made after the profits have been ascertained and become liable to taxation, and the payment to Bai Tarabai is nothing more than a mere distribution of part of the profits.

It is contended by Mr. Setalvad that the payment to Bai Tarabai is a payment out of the profits and conditional on profits being earned, and strong reliance is placed on the statement of Lord Macmillan in the *Pondicherry case*[1] :—

"A payment out of profits and conditional on profits being earned cannot accurately be described as a payment made to earn profits. It assumes that profits have first come into existence. But profits on their coming into existence attract tax at that point and the revenue is not concerned with the subsequent application of the profits."

But this statement of Lord Macmillan has been the subject of considerable comment in subsequent cases. As I shall presently point out, the principle was enunciated by Lord Macmillan in rather wide terms and subsequent cases have definitely laid down that this particular observation of the learned law Lord should be read in, and confined to, its own context. In *Union Cold Storage Co., Ltd.* v. *Adamson*[2], the assessee company claimed that the rent it paid on lands and premises leased by it should be allowed as a deduction. There was a provision in the agreement that the rent payable bore some relation to the profits earned by the company. The House of Lords held that the payments were not payable out of the profits or gains and that they were allowable deductions. Lord Macmillan was at pains in this case to explain the observations he had made in the *Pondicherry case*[1] to which I have referred and he was careful to observe that that particular observation applied to the facts found in that case; and Lord Maugham in the *Indian Radio and Cable Communications Company's case*[3], expressly stated that it was not universally true to say that a payment, the making of which was conditional on profits being earned, could not properly be described as an expenditure incurred for the purpose of earning such profits. He further observed that the difficulty mainly arose because the word "profits" was used in more than one sense. He points out that if a company makes a net profit of £ 10,000 and has then to pay £ 1,000 to directors or managers for services rendered £ 10,000 are only the apparent profits, but the real profits are £ 9,000.

Therefore in every case the Court has got to consider what are the real profits of the assessee and what are the apparent profits. It is only the real profits that attract the tax; and even though the language used in the material documents may be "net profits," the Court must look to the substance of the transaction and not the form. In this case the two documents I have referred to provide that Bai Tarabai has got to be paid two annas in the rupee of the "net profits." But the two annas in the rupee have to be

(1) (1931) 5 I.T.C. 363, at p. 370.
(2) (1931) 16 Tax Cas. 293.
(3) [1937] 5 I.T.R. 270, at p. 277.

paid for the use of the goodwill which is essential for the carrying on of the business. Therefore first the apparent profits of the partnership are ascertained and two annas in the rupee are paid out to Bai Tarabai out of those profits; and after those payments are made, the real profits are ascertained which attract the tax; and it is these real profits that are distributed among the partners in the proportion laid down in the partnership agreement, making up what is described as a unit of 14 annas.

The observation of Lord Macmillan in the *Pondicherry case*[1] was again considered in *British Sugar Manufacturers, Ltd.* v. *Harris*[2]. In this case a company carrying on a manufacturing business agreed with two other companies to pay them a stated percentage of its net profits. "Net profits" were to be ascertained after payment of all expenses of the company and after providing for interest on debentures, but before making any provisions for depreciation. The Court of Appeal held that in computing its profits for the purposes of income-tax, the company was entitled to deduct the sums so paid as being "money wholly and exclusively laid out or expended for the purposes of the trade." Lord Greene, the Master of the Rolls, pointed out that the "net profits" were to be arrived at upon a conventional basis, not the basis upon which the company would ascertain its profits for commercial purposes or the basis upon which it would ascertain its profits for income-tax purposes; and the percentage was to be paid out of these conventional profits and not the profits which were liable to tax. In the case before us also Bai Tarabai receives two annas in the rupee out of a fund which, although described as net profits, is really an artificial fund ascertained for the purpose of giving to Bai Tarabai her share under the agreement. The Master of the Rolls also appreciated the difficulty of distinguishing cases which are for a payment of a share of profits *simpliciter* and a payment of remuneration which is deductible in truth before the profits divisible are ascertained; and he confesses that the line between these two classes of cases was very difficult to draw. The Master of the Rolls further made it clear that the observations of Lord Macmillan in the *Pondicherry case*[1] referred to profits in the sense of real net profits.

This High Court, in *Commissioner of Income-tax, Bombay* v. *C. Macdonald and Company*[3], applied the principle of the *Pondicherry case*[1]. In that case the assessees as the managing agents of a company received the sum of Rs. 97,000. From this amount they paid Rs. 19,000 odd to third parties under certain agreements to pay them a proportion of the gross income and they claimed that in assessing their profits they were entitled to have a deduction of this sum of Rs. 19,000 odd from the amount of Rs. 97,000 received by them. The Court of Appeal (*sic*) rejected their contention. But it is to be noted that the learned Chief Justice, Sir John Beaumont, expressly points out in his judgment that it had not been argued

(1) (1931) 5 I.T.C. 363.
(2) [1939] 7 I.T.R. 101.
(3) [1935] 3 I.T.R. 459.

that the sums paid to third parties came within any of the various deductions allowed by the Indian Income-tax Act. On the other hand, the High Court in *Commissioner of Income-tax, Bombay Presidency v. Tata Sons Limited*[1] held that the payment to a financier of the share of the commission earned by Tata Sons Limited in order to obtain finance for the purposes of financing the Tata Iron and Steel Company Limited was an expenditure incurred by the assessees solely for the purposes of earning their profits and was a permissible deduction. Sir John Beaumont frankly confessed that in the past he had wrongly understood the principle of the *Pondicherry case*[2]; but the subsequent decisions had made the position clear. He observes that the question whether the payment of part of a commission to a third person can be regarded as expenditure incurred solely for the purpose of earning that commission is a question which must be answered on the facts of each case and on a commercial basis.

It has been further contended by Mr. Setalvad that the agreement between Bai Tarabai and the partners of the firm is in the nature of a joint adventure or a quasi partnership and, therefore, what Bai Tarabai and the partners of the firm are doing are really sharing the real profits of the firm. Emphasis has been laid on the remarks of Lord Maugham in delivering the judgment of the Judicial Committee in *Indian Radio and Cable Communications Company Ltd.* v. *Commissioner of Income-tax, Bombay Presidency and Aden*[3]. In that case the assessee company agreed to pay one-half of its net profits to another company in consideration of certain advantages to be received by the assessee company from the other company. The assessee company contended that the payment of share of the net profits was in the nature of rent and, therefore, it was entitled to deduct it from its net profits. The contention of the assessee company was rejected by the Privy Council. Lord Maugham pointed out that the one-half share of the profits was made payable as part of the consideration in respect of a number of different advantages which the assessee derived from the agreement and not all of them was shown to be of a purely temporary character and, therefore, the Privy Council came to the conclusion that the agreement as a whole was much more like one for a joint adventure for a term of years between the assessee company and the other company.

It is impossible to contend that in the case before us the partnership is receiving a number of advantages from Bai Tarabai. The agreement between the firm and Bai Tarabai is a simple one and all that the partnership is doing is paying an amount fixed by reference to profits as a fee or charge for the use of the goodwill granted to it by Bai Tarabai. In our opinion it would not be correct to say that this agreement is in the nature of a joint adventure or a quasi partnership.

(1) [1939] 7 I.T.R. 195.
(2) (1931) 5 I.T.C. 363.
(3) [1937] 5 I.T.R. 270.

Finally it was argued by Mr. Setalvad that the amount paid by the partnership firm to Bai Tarabai is not an expenditure expended wholly and exclusively for the purposes of the business. It is urged that this amount was not paid for the purposes of producing profits in the conduct of the business, but was paid in order to acquire the right to conduct the business in the particular name. It is not possible to accept this contention. The name in which a business is carried on is an important factor and the reason why the partnership paid for the goodwill was in order to attract more customers and earn more profits. The observations in the judgment delivered by Lord Macmillan in the *Tata Hydro-Electric Agencies case*[1], must be read in the light of the facts found in that case; he said: —

"In short, the obligation to make these payments was undertaken by the appellants in consideration of their acquisition of the right and opportunity to earn profits, that is, of the right to conduct the business, and not for the purpose of producing profits in the conduct of the business."

In that case Tata Sons Limited, who were the managing agents of Tata Power Company Limited, assigned the agency agreement to the assessees, Tata Hydro-Electric Agencies Limited. The Tata Power Company entered into a new agreement with the assessees on terms identical with their agreement with Tata Sons Limited whereby they agreed to pay to Tata Hydro-Electric Agencies Limited a commission of 10 per cent. on the annual net profits of the Tata Power Company. The assessee company entered into an agreement with two financiers D and S and agreed to pay each of them $12\frac{1}{2}$ per cent. of the commission earned by them from the Tata Power Company. The assessee company claimed one-fourth of the amount of the commission earned by them and paid to D and S as an allowable deduction. Their contention was rejected by the Privy Council. It is important to note that it was found as a fact that the assessee company had agreed to pay a share in the commission to D and S whether the business of the assessee company yielded any profit or not, and as the share in the commission was to be paid irrespective of whether profits were made or not, the Privy Council found it difficult to hold that the payment was made solely for the purposes of earning the profits of the business. It will also be remembered that in the case of *Ogden* v. *Medway Cinemas, Limited*[2], to which we have referred earlier, Mr. Justice Finlay held that the payment for goodwill was a necessary revenue expense of the company.

In our judgment the sum paid to Bai Tarabai is an item of revenue expenditure and admissible for deduction under Section 10 (2) (*xii*) of the Income-tax Act. Accordingly the first question referred to us must be answered in the negative and the second question in the affirmative.

The Commissioner must pay the costs throughout.

Reference answered accordingly.

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(1) [1937] 5 I.T.R. 202, at p. 209. (2) (1934) 18 Tax Cas. 691.

SUPPLEMENT

TO

THE

INCOME TAX REPORTS

VOLUME XIV

CONTAINING

SELECT ENGLISH CASES

[IN THE HOUSE OF LORDS.]

INLAND REVENUE COMMISSIONERS *v.* BYRON, LTD.

THE LORD CHANCELLOR (VISCOUNT SIMON), LORD RUSSELL OF KILLOWEN, LORD PORTER, LORD SIMONDS.

Feb. 26, 27, 28; March 28; May 17, 1945.

EXCESS PROFITS TAX—COMPANY THEATRE PROPRIETORS—THEATRE DESTROYED BY ENEMY ACTION—EFFECT ON COMPANY'S CAPITAL—WHETHER FREEHOLD SITE AND RUBBLE "CAPITAL EMPLOYED IN THE SAME TRADE OR BUSINESS"—FINANCE (NO. 2) ACT, 1939 (2 & 3 GEO. 6, c. 41), s. 13 (3), SEVENTH SCHEDULE.

The respondent company carried on business as theatre proprietors, and in April, 1937, bought the A. Theatre at Hull for £ 12,280. On May 7, 1941, the theatre was destroyed by enemy action. The freehold site continued to belong to the company. The Crown contended that there had been a decrease in the average amount of the capital employed in the respondents' business in the accounting period ending May 28, 1941, and that the standard profits should therefore be decreased in relation to that accounting period by the statutory percentage of 6 per cent. on the decrease of capital, and that the company was left with a new and different asset from the asset it acquired for £ 12,280 in April, 1937 :—Held, *that under the provisions of the Seventh Schedule of the Finance (No. 2) Act, 1939, the value of an asset was fixed as being the price at which the asset was acquired, subject only to the deductions mentioned in paragraph 2, and, therefore, so long as the asset remained part of the capital employed in the trade or business, the value to be put upon it for the purpose of calculating excess profits tax was not to be decreased when the asset was no longer, owing to change of circumstances, worth its original value. The asset, as it*

was after enemy action, was not a new and different asset. The freehold site and what was still upon it was "capital employed in the trade or business" within the meaning of Section 13 (3) of the Act of 1939.

Decision of the COURT OF APPEAL (60 T.L.R. 367) *affirmed.*

Cases referred to:

Merlimau Rubber Estates, Ltd. *v.* Inland Revenue Commissioners [1923] (92 L.J.K.B. 504; [1923] A.C. 283).

Sungei Rubber Co. *v.* Inland Revenue Commissioners [1925] (94 L.J.K.B. 865).

Appeal from the Court of Appeal.

The material facts are stated in the headnote.

The Attorney-General (*Sir Donald Somervell, K.C.*), and *Reginald Hills*, for the appellant Commissioners.

F. Heyworth Talbot, for the respondent company.

The arguments appear from the judgment.

Their Lordships took time for consideration.

LORD SIMON.—This is an appeal from an order of the Court of Appeal (Scott, L.J., Goddard, L.J., and du Parcq, L.J.), dated May 4, 1944, dismissing an appeal by the appellants from an order of the King's Bench Division (Macnaghten, J.), dated July 20, 1942, whereby an appeal on a case stated by the Commissioners for the General Purposes of the Income Tax for the Stockport Division of the county of Chester was dismissed and the decision of the Commissioners was affirmed. The facts, which are quite short, give rise to a difficult question as to the interpretation and application of Sections 13 (3) and 14 (2) of the Finance (No. 2) Act, 1939, in respect of the calculation of the average amount of the capital employed in the trade or business of the respondent company in the chargeable accounting period ending May 28, 1941, for the purpose of an assessment to excess profits tax on the profits of the company's business in that accounting period.

The excess profits tax is charged upon the excess of profits arising in the chargeable accounting period over the standard profits, and standard profits are computed in accordance with Section 13 of the Act. Generally speaking, therefore, once the standard profits have been correctly computed, all that remains to be done in a case where the profits in an accounting period have risen beyond this figure is to charge the prescribed rate of tax on the excess; and thus, in an ordinary case, no question of calculating the capital employed in the trade or business arises. If, however, the average amount of the capital employed in the trade or business in the accounting period is greater, or less, than the average amount of the capital employed therein in the standard period, an adjustment has to be made. If the average amount of such capital is greater than in the standard period, the standard profits are increased in relation

to that chargeable accounting period, and, if the average amount of such capital has decreased, the standard profits are, in relation to that chargeable accounting period, decreased by the appropriate statutory percentage. In the case of an increase in the average amount of capital in an accounting period, the statutory percentage by which the standard profits are increased is 8 per cent. or 10 per cent. of the excess, as prescribed in sub-section (9) of Section 13. If the average amount of capital employed in the trade or business in the accounting period is less than the average amount employed therein in the standard period (and this is the case which is said to arise in the present appeal), the reduction in standard profits is arrived at by deducting 6 per cent. of the amount of the decrease. Some such adjustment of figures is manifestly necessary if the tax is to be equitably applied to a business the capital of which varies, for, with an increased capital, the business may be expected (if conditions remain otherwise the same) to make an increased profit, which, none the less, would not necessarily indicate an excess in the rate of profit made as compared with the standard profit.

The respondent company was incorporated in June, 1934, with the object, *inter alia*, of carrying on business as theatre, music-hall and cinema proprietors. At all material times it carried on the business of theatre proprietors at five theatres of which it was the lessee, and, until May 7, 1941, also at the Alexandria Theatre, Hull, of which it became the owner in April, 1937, by purchase at a total price of £12,280. This theatre was destroyed by enemy action on May 7, 1941. The freehold site continues to belong to the respondents.

In these circumstances the appellants contend that there has been a decrease in the average amount of the capital employed in the respondents' business in the accounting period ending May 28, 1941, and that the standard profits should therefore be decreased in relation to that accounting period by the statutory percentage of 6 per cent. on the decrease of capital. The respondent company, on the other hand, contends that, notwithstanding the destruction of the theatre, there has been no decrease in the capital employed in its business, and therefore that no reduction in the figure of standard profits is justified. This latter contention has hitherto prevailed at every stage of the present litigation.

Part II of the Seventh Schedule of the Finance (No. 2) Act, 1939, contains provisions for computing capital for the purposes of excess profits tax, and the question in dispute must be decided in the light of these provisions. An inspection of the terms of this Schedule shows clearly that the capital employed in a trade or business is not what, in other connections, might properly be described as the total capital, but

is arrived at conventionally according to the rules laid down in the Schedule for the purpose. Paragraph 1 of these provisions is as follows: "1.—(1) Subject to the provisions of this Part of this Schedule, the amount of the capital employed in a trade or business (so far as it does not consist of money) shall be taken to be—(a) so far as it consists of assets acquired by purchase on or after the commencement of the trade or business, the price at which those assets were acquired, subject to the deductions hereafter specified; (b) so far as it consists of assets being debts due to the person carrying on the trade or business, the nominal amount of those debts, subject to the said deductions; (c) so far as it consists of any other assets which have been acquired otherwise than by purchase as aforesaid, the value of the assets when they became assets of the trade or business, subject to the said deductions. (2) The price or value of any assets other than a debt shall be subject to the following deductions—(a) a deduction of any sum contributed, directly or indirectly, out of the Consolidated Fund of the United Kingdom or of Northern Ireland, or out of moneys provided by the Parliament of the United Kingdom or the Parliament of Northern Ireland, towards the acquisition of the asset; (b) any such deductions for wear and tear or for depreciation as are authorised by the Income Tax Acts or Part I of this Schedule, and, in the case of a debt, the nominal amount of the debt shall be subject to any deduction which has been allowed in respect thereof for income tax purposes. (3) Where the price of any asset has been satisfied otherwise than in cash, the then value of the consideration actually given for the asset shall be treated as the price at which the asset was acquired."

What is particularly noteworthy in the above provisions of the Schedule is that the value of an asset, whether acquired by purchase or otherwise, is fixed as being the price at which the asset was acquired, or the value of the asset when it became an asset of the trade or business, subject only to the deductions mentioned in sub-paragraph (2). So long as the asset remains part of the capital employed in the trade or business, it would appear, therefore, that the value to be put upon it for the purposes of calculating excess profits tax is not to be increased with the increase of its real value, and, equally, that changes of circumstances which in fact render the asset no longer worth its original value do not affect the value to be put on the asset for excess profits tax purposes. In these respects, as well as in others, the valuation of capital under the Schedule for the purpose of calculating the tax is manifestly different from the valuation which would be proper in a balance-sheet or in the application of company law.

The Attorney-General and his junior contended that the destruction of the Hull theatre by enemy action left the respondent company with a new and different asset from the asset which they had acquired by purchase at the price of £ 12,280 in April, 1937. According to this argument, the site with the ruins of the theatre upon it is a different asset from the theatre which was bought. The Crown pointed out that previous decisions had recognised the possibility of an asset acquired by purchase and falling within paragraph 1 (1) (a) of the Schedule being so transformed that it is regarded as becoming a different asset and falling within paragraph 1 (1),(c). For example, under the analogous provisions of the former excess profits duty, in *Merlimau Rubber Estates, Ltd.* v. *Inland Revenue Commissioners*[1], where a property bought by the appellant was an undeveloped rubber estate which, as the result of further expenditure and cultivation, became in time a fully productive rubber estate, it was contended that the treatment of the estate had the effect of transforming it into a new asset, so that the property was no longer to be valued under paragraph (a), but was converted into a new asset falling into paragraph (c). The contention did not succeed, but Lord Wrenbury took the view that such a transformation was a possibility, and that it was a question of fact whether what had happened since the original purchase had resulted in the disappearance of the old asset and the creation of another asset in its place. Lord Wrenbury illustrated his meaning by saying (92 L.J.K.B., at p. 508 ; [1923] A.C., at p. 291) that " if a man buys a quarter of an acre of land and builds a house upon it, he does not continue the owner of the bare land within (*a*) and become the owner of another asset—namely, a house, upon the land within (*c*). A house cannot exist except in conjunction with the land on which it stands. The land was within (*a*), but when the house was built the land, so to speak, ceased to be in (*a*) and the owner became entitled to a new asset—namely, the house with the land on which it stood within (*c*)." Lord Buckmaster was not prepared to say that in certain circumstances this sort of transformation might not take place, but he found it unnecessary to decide the question, because he and the other members of the House all came to the conclusion that in fact no sufficient transformation had taken place in that case to produce such a result.

The matter was carried a little further in *Sungei Rubber Co.* v. *Inland Revenue Commissioners*[2], which was a case where the company had bought virgin jungle, and, as a result of large expenditure and the planting of trees, had turned it into a valuable rubber plantation. It

(1) (1923) 92 L.J.K.B. 504 ; [1923] A.C. 283. (2) (1925) 94 L.J.K.B. 865.

was held, first by Rowlatt, J., and then by the Court of Appeal, that the rubber estate was a different asset from mere virgin jungle, and that the company had, therefore, acquired a new asset which would be valued under paragraph 1 (*c*), and not under paragraph 1 (*a*).

Adopting the principle involved in the *Sungei Rubber Co.'s case* [1], the Crown here argues that the asset which the respondent company bought at the price of £12,280 was a theatre, and that what it has been left with, as the result of enemy bombing, is a different asset, namely, the site with rubble upon it. I do not think that this is the proper view to take of the facts in this particular case, and in my opinion the company still has the asset which it originally bought, though the asset has been very much damaged by enemy action. If, instead of being laid waste by bombing, the theatre had been less severely damaged, for example, if a portion of it had been struck by lightning or consumed by fire, it could hardly be said that the asset originally bought had been turned into something else. The company in fact bought the freehold site with a valuable building upon it, and what has happened since does not produce the result that the company no longer owns the asset and in its place has acquired a new one. All that has happened is that, while the original asset continues to be owned by the company, its value has been greatly reduced by the damage which has occurred. On this view of the facts the value that must be attributed to the asset for the purposes of the tax is the price originally paid for it, and there is no decrease in the capital when the capital is computed in accordance with the Seventh Schedule. The Crown put forward, as an alternative contention, the view that the damage which had occurred produced the result that whatever capital the company previously had at Hull was no longer "employed in its trade or business." In my opinion, this contention is not sound. The fact that the Hull building has been so much damaged that it cannot at present be used as a theatre does not seem to me in itself to establish that the freehold site and what is upon it is not still "employed in the trade or business." If the company decided to abandon the use of the site for the purpose of its business, different considerations might arise. If, however, the theatre was for other reasons temporarily closed, or if it was in course of reconstruction and improvement, this would not justify the contention that it formed no part of the capital referred to in Part II of the Seventh Schedule. Even if it be the case that, for the purposes of excess profits tax, the capital employed in a trade or business of a company does not necessarily include all the capital of the company (and it certainly expressly excludes investments held by

(1) (1925) 94 L.J.K.B. 865.

a company, the income from which is not to be taken into account in computing the profits of the trade or business (Seventh Schedule, Part II, para. 3)), the asset at Hull must be regarded as still employed in the trade or business, even though it is not actively or productively employed in the accounting period.

I have not thought it necessary to discuss the further argument of the respondent company that, even if the damaged site at Hull were to be regarded as a new asset, it is an asset which must be valued after taking into account the fact that the company have a war-damage claim in respect of it, which (as was conceded) would leave the company's asset with an actual value not less than that attached to it before the bomb fell.

In my opinion, this appeal should be dismissed. The facts of the case do not support the contentions of the Crown, and it is not necessary for the House to pronounce upon some of the difficult matters of a more general character which in another case might have to be explicitly decided.

I move that the appeal should be dismissed with costs.

The Lord Chancellor.—My noble and learned friend Lord Macmillan, who is not able to be present, authorises me to say that he agrees with the opinion which I have just delivered, and that he has nothing to add.

Lord Russell of Killowen.—I also agree with the opinion which has just been delivered by the noble and learned Lord on the Woolsack.

Lord Porter.—I had prepared a speech in this matter, but, having heard the speech of the noble and learned Lord upon the Woolsack, I find it unnecessary to trouble your Lordships, as I entirely agree with the views expressed by him.

Lord Simonds.—I also concur. *Appeal dismissed.*

[In the House of Lords.]

INLAND REVENUE COMMISSIONERS v. BIBBY & SONS, LTD.

Lord Russell of Killowen, Lord Macmillan, Lord Wright, Lord Porter, Lord Simonds.

March 15, 19; May 17, 1945.

Excess Profits Tax—Company—Directors Having "Controlling Interest"—Shares Held by Some Directors as Trustees—Such Shares Also Giving Control—Finance (No. 2) Act, 1939 (2 & 3 Geo. 6, c. 109), Sec. 13 (9) (b).

The preference shares of a company carried no votes, but each ordinary share carried one vote on a poll. There were eight directors, who were respectively beneficial owners and registered holders of ordinary shares, amounting to 209,332 shares. Three of the directors were registered as joint holders of 57,500 other ordinary shares, which they held as trustees of their sister's marriage settlement, under the trusts of which they were entitled to a contingent reversionary interest in the shares. If these trustee shares were not to be taken into account in considering whether the directors had a controlling interest in the company, the company's business fell within Section 13 (9) (a) of the Finance (No. 2) Act, 1939, and the company were only entitled to an increase of 8 per cent. But if the trustee shares were to be taken into account the company's business would then fall within sub-section (9) (b) of Section 13, and it could claim an increase of 10 per cent.:—
Held, *that the test which was to exclude a company's business from sub-section (9) (a), and include it in sub-section (9) (b), was the voting power of its directors, not their beneficial interest in the company. The words "controlling interest" meant controlling voting power; that was the interest in view, not beneficial interest. No definite opinion given as to the case where a trustee was a bare trustee.*

Decision of the Court of Appeal (60 T.L.R. 369) *affirmed.*

Cases referred to:—

British American Tobacco Co. *v.* Inland Revenue Commissioners [1942] (112 L.J.K.B. 81; [1943] A.C. 335; 11 I.T.R. Suppl. 29)

City of London Income Tax Commissioner *v.* Gibbs [1942] (111 L.J.K.B. 301; [1942] A.C. 402).

Muir *v.* City of Glasgow Bank [1878] (4 App. Cas. 337; 40 L.T. 339).

Puddephatt *v.* Leith [1915] (85 L.J. Ch. 185; [1916] 1 Ch. 200).

Pulbrook *v.* Richmond Consolidated Mining Co. [1878] (48 L.J.Ch. 65; 9 Ch. D. 610).

Appeal from the judgment of the Court of Appeal.

The facts are stated in the headnote.

The Solicitor-General (*Sir David Maxwell Fyfe, K. C.*), *J. H. Stamp* and *Reginald Hills*, for the appellants.

Tucker, K. C., Scrimgeour and *Terence Donovan*, for the respondents.

The arguments sufficiently appear in the judgments.

Their Lordships took time for consideration.

LORD RUSSELL OF KILLOWEN.—This appeal arises out of an assessment to excess profits tax of the respondent (which I will refer to as the company), the dispute being whether the company is entitled to have its standard profits increased by 10 per cent., or only by 8 per cent. The decision depends upon the answer to the question whether the company is or is not "a company the directors whereof have a

controlling interest therein," within the meaning of Section 13 (9) of the Finance (No. 2) Act of 1939.

The only relevant facts (and they are not in dispute) are these: The company's issued capital consists of 750,000 £1 preference shares and 500,000 £1 ordinary shares. The preference shares carry no votes. Each ordinary share carries one vote on a poll. There are eight directors, who are respectively beneficial owners and registered holders of ordinary shares, which amount to a total of 209,332 shares. Three of the directors are registered as joint holders of 57,500 other ordinary shares, which they hold as trustees of their sister's marriage settlement, under the trusts of which they are entitled to a contingent reversionary interest in the shares. Upon these facts it is apparent that, if these trustee shares are not to be taken into account in considering the question whether the directors have a controlling interest in the company, the answer must be that the company is only entitled to an increase of 8 per cent. Its business falls within Section 13 (9) (*a*). If the trustee shares are to be taken into account the answer would seem equally clear. The company's business would then fall within sub-section (9) (*b*), and it can claim an increase of 10 per cent.

Macnaghten, J., affirming the decision of the Special Commissioners, held that the trustee shares must be excluded from consideration. His opinion was thus expressed: "As trustees they have no 'interest' in the shares; and as beneficiaries they have no 'control' over the company; and therefore, in order to ascertain whether the directors of the company have a controlling interest therein, the shares held by them as trustees must be excluded." This, as I read it, means that the control must be derived solely from voting power attached to shares which are held by the directors and of which the directors are the absolute beneficial owners. The Court of Appeal took a different view, being of opinion that there was no justification for limiting the phrase "controlling interest" in Section 13 to the case of beneficial interests, and that shares held by the directors as trustees must be taken into account. Further they were of opinion that the possession by the directors of some beneficial interest in the shares of which they were trustees was an irrelevant fact. I quote their words: "It appears to us that, apart from the special case of a bare trustee, there is no half-way house between an interpretation which limits the expression to the case of beneficial ownership, and one which includes ownership by trustees irrespective of the fact whether or not they also have some beneficial interest in the shares which give control."

I agree with the view of the Court of Appeal. When the section speaks of directors having a controlling interest in a company, what

it is immediately concerned with in using the words "controlling interest" is not the extent to which the individuals are beneficially interested in the profits of the company as a going concern or in the surplus assets in a winding-up, but the extent to which they have vested in them the power of controlling by votes the decisions which will bind the company in the shape of resolutions passed by the shareholders in general meeting. In other words, the test which is to exclude a company's business from sub-section (9) (*a*), and include it in (9) (*b*), is the voting power of its directors, not their beneficial interest in the company.

For the purpose of such a test the fact that a vote-carrying share is vested in a director as trustee seems immaterial. The power is there, and, though it be exercised in breach of trust or even in breach of an injunction, the vote would be validly cast *vis-a-vis* the company, and the resolution until rescinded would be binding on it. The contention that upon the wording of Section 13 the interest must be confined to beneficial interests appears to me to be but a repetition of the argument which was rejected by this House in the case of *British American Tobacco Co.* v. *Inland Revenue Commissioners*[1] in relation to National Defence Contribution and the Finance Act, 1937. It may be that, as the appellants contended, an object of the sub-section now in question was to compensate a director-controlled company for the disability imposed on it by paragraph 10 of Part I of the Seventh Schedule to the Act, but I cannot deduce from this fact, if it be a fact, that controlling interests must be confined to beneficial interests which give control. I agree with the view of the Court of Appeal that upon the true construction of Section 13 (9), standing alone, there could be no justification for so restricting the words, or reading into the sub-section a provision to the effect that control held as a trustee should be disregarded.

A long and detailed argument was, however, addressed to us based upon other sections of the 1939 Act, and some provisions of the Finance Act, 1937, in which the phrase "the directors whereof have a controlling interest therein" occurs, and in which it was contended that the word "interest" was necessarily limited to a beneficial interest. Therefore, it was said, the word must be so limited in Section 13 (9). Thus, the provisions in paragraphs 4 (*b*), 7 (*b*), 11 and 12 of the Fourth Schedule to the Finance Act, 1937, were relied upon for this purpose. They are provisions which (to put it shortly) prohibit or restrict the permissible amount of deductions from profits in the case of companies "the directors whereof have a controlling interest therein." The

1) (1943) 11 I.T.R. Suppl. 29; [1943] A.C. 335.

deductions, being deductions in respect of payments which the company would be making to the directors or some or one of them for their or his own beneficial enjoyment (for example, for remuneration or rent), it follows, so it was contended, that the controlling interest must also be one enjoyed by them beneficially. With all respect to those who advance this argument, I can only answer "*non sequitur.*" I can find in it no compulsion so to restrict the meaning of the words "controlling interest." Reliance was also placed on Section 13 (2) (*b*) of the Finance (No. 2) Act, 1939, in which, it was said, the phrase "owning not less than one-fifth of the share capital" could not mean owning as trustee, and therefore the controlling interest referred to earlier in the sub-section could not refer to an interest owned as trustee. I am not prepared, as at present advised, to concede the first part of this proposition. Director-controlled companies are as a rule private companies in which trustee directors are a not uncommon feature, just as in partnerships one may find a partner who, as the representative of a deceased former partner, is carrying on the business, for the benefit of beneficiaries, in partnership with a surviving partner.

Much reliance was placed on the provisions contained in paragraph 10 of Part I of the Seventh Schedule to the Finance (No. 2) Act, 1939. The argument founded thereon is fully stated and dealt with in the judgment of the Court of Appeal. I need only say that I agree with the criticism and conclusion contained in that judgment. I agree also with the sympathy expressed with the taxpayer who (according to the appellants) has to discover the true meaning of Section 13 (9) of the Finance (No. 2) Act, 1939, by a close scrutiny and analysis of other provisions of that and other Finance Acts. If his scrutiny and analysis were sufficiently close he might notice that sub-paragraph (2) of the same paragraph 10 suggests that a registered shareholder who is not a beneficial owner may directly control ordinary shares, and he might perhaps wonder, on reading the Finance Act, 1940, why the Legislature had not inserted in the 1939 Act a provision similar to that which is contained in Section 55 (5) of the Act of 1940.

Counsel for the appellants, at one stage of the argument, suggested that shares registered in the name of a director but held by him as trustee might be included in reckoning the controlling interest in cases where the trustee had also what was described as a predominating beneficial interest in the shares. For myself, I am unable to appreciate how these supposed different degrees of beneficial interest, or the existence in the trustees of any beneficial interest, can affect the question of control. The words "controlling interest" mean "controlling voting power"; that is the interest in view, not beneficial interest. As

at present advised, I agree with the Court of Appeal in the view that there is no half-way house between a construction which restricts the controlling interest to shares which are in the absolute beneficial ownership of the trustees and a construction which includes all shares of which the directors are registered holders. It is true that the Court of Appeal except the case of what they describe as a bare trustee, but express a view that the control would reside in the beneficial owner of the shares. The case envisaged is, no doubt, the case of the director who puts shares into the name of a nominee, taking probably a blank transfer executed by the nominee. I prefer to express no definite opinion in relation to this question, but to keep it as an open question to be debated when the necessity for a decision thereon in fact arises.

I would dismiss this appeal with costs to be taxed as between solicitor and client in accordance with the undertaking given by the appellants to the Court of Appeal.

LORD RUSSELL OF KILLOWEN.—My Lords, my noble and learned friend Lord Wright, who is unable to be present to-day, has asked me to say that he concurs in the opinion which I have just delivered.

LORD MACMILLAN (read by LORD PORTER).—The question is whether the directors of the respondent company have "a controlling interest therein" within the meaning of Section 13 (9) (*a*) of the Finance (No. 2) Act, 1939. The answer will affect the extent of the company's liability to excess profits tax for the chargeable accounting period from April 1 to December 31, 1939. The company employed in its business in that period an average amount of capital greater than the average amount employed in the standard period, and is therefore entitled to have its standard profits increased by a statutory percentage of the increase in its capital. If the directors have a controlling interest in the company, the statutory percentage applicable is 10 per cent.; if not, the statutory percentage applicable is 8 per cent.

The control of a company resides in the voting power of its shareholders. In the respondent company the ordinary shares alone confer a right to vote at a general meeting. The directors are the registered proprietors of a majority of the ordinary shares. It would therefore appear to follow that the directors have a controlling interest in the company. The appellants, however, maintain that this is not so, for the reason that certain of the ordinary shares held by three of the directors are held by them as trustees under the marriage settlement of their sister. The contention is that these trust shares must, on a sound interpretation of the statute, be excluded from the reckoning for the present purpose, because the directors in question have not the sole, or at least not a predominant, beneficial interest in them. It is agreed

that if these shares be excluded, then the directors do not among them hold a majority of the ordinary shares and so do not have a controlling interest in the company.

In my opinion, the Court of Appeal rightly rejected the contention of the Inland Revenue Commissioners. The question whether the directors of the respondent company have the control of it by their voting power as shareholders must, in my view, be determined by the memorandum and articles of the company and by the register of shareholders. By the constitution of the company, as I have already mentioned, the voting power is vested in the ordinary shareholders, and the register shows that the directors hold a majority of these shares. As was said by Jessel, M.R.: "The company cannot look behind the register as to the beneficial interest, but must take the register as conclusive, and cannot inquire, . . . into the trusts affecting the shares" (*Pulbrook* v. *Richmond Consolidated Mining Co.*[1]). So far as the company is concerned the relation between such of its shareholders as happen to be trustees and their beneficiaries is *res inter alios*. It may be that a trustee shareholder may, as between himself and his *cestuis que trust*, be under a duty to exercise his vote in a particular manner, or a shareholder may be bound under contract to vote in a particular way (*Puddephatt* v. *Leith*[2]). But with such restrictions the company has nothing to do. It must accept and act upon the shareholder's vote, notwithstanding that it may be given contrary to some duty which he owes to outsiders. The remedy for such breach lies elsewhere. Suppose that all the shares held by the directors in the present case were held by them as trustees, could it be said that they did not control the company? If so, then in whose hands was the control of the company?

The learned Solicitor-General, in maintaining that the statutory words "a company the directors whereof have a controlling interest therein" should be expanded by the addition of the words "by reason of their being the beneficial owners in the aggregate of shares entitling them to a majority of votes," submitted that the reason for the legislation justified this implication. The extra 2 per cent., he said, was by way of compensation for the restriction imposed elsewhere in the Act on the diversion of profits by directors to their own remuneration, but as it would be improper for trustee shareholders to vote for an increase in their remuneration as directors, at least without the consent of their beneficiaries, there was not the same need for the restriction in their case. This may be so, but I do not think that it is a sufficient justification for so extensive a qualification of the plain words of the

(1) (1878) 48 L.J. Ch. 65; 9 Ch. D. 610. (2) (1915) 85 L.J. Ch. 185; [1916] 1 Ch. 200.

statute. Your Lordships were also referred to other instances of the use of the phrase "controlling interest" elsewhere in the Act, and also in the Finance Act of 1937, as supporting the Crown's contention. But this proved rather double-edged, for in one instance in the 1939 Act there occurs the expression "the beneficial owner of . . . more than 5 per cent. of the ordinary share capital of the company" [Seventh Schedule, Part I, para. 10 (2)], which at least suggests that when the Legislature means beneficial ownership it knows how to say so. I remain unconvinced by this line of argument. It so happens that the three directors in question have a remote contingent beneficial interest in the trust for which they hold shares. In the view which I take this is immaterial, but if beneficial interest were necessary, then, unless beneficial interest were taken to mean sole beneficial interest, I can conceive complicated questions arising as to the extent of the beneficial interest of the shareholder in particular cases, which would be unfortunate for the working of an emergency taxing measure.

I would only add that I have not overlooked the fact that this legislation applies to Scotland as well as to England, and that in Scotland trustee shareholders are registered as such. The Act should, if possible, receive an interpretation which will be equally applicable on both sides of the border. "In construing a taxing statute which applies to England and Scotland alike, it is desirable to adopt a construction of statutory words which avoids differences of interpretation of a technical character such as are calculated to produce inequalities in taxation as between citizens of the two countries" (*City of London Income Tax Commissioners* v. *Gibbs*[1], *per* Simon, L. C.). I find no reason in the circumstances to which I have alluded for thinking that it would lead to a different result in Scotland. The reason why in Scotland trustees as such are entered in the share register is very fully explained in the case of *Muir* v. *City of Glasgow Bank*[2] by Lord President Inglis in the Court of Session and Cairns, L.C., in this House. It would be inappropriate to go into the matter here. Suffice it to say that so far as his position *vis-a-vis* the company is concerned the trustee shareholder whose name appears as such in the register is, as regards his rights and liabilities, in exactly the same position as a shareholder who is not a trustee.

I am, accordingly, in agreement with your Lordships that this appeal should be dismissed.

LORD PORTER.—I have had an opportunity of reading and agree with the opinions of my noble and learned friends Lord Russell of Killowen and Lord Simonds. I cannot doubt that by the expression "a

(1) (1942) 111 L.J.K.B. 301; [1942] A.C. 402. (2) (1878) 4 App. Cas. 337.

company the directors whereof have a controlling interest therein" is meant a company in which the directors by means of their shareholding are able to direct the affairs of the company according to their will. This is, in my view, the natural meaning of these words. It was, however, argued that if one looked at the object of the Act and searched its phraseology one would find that they bore the narrower meaning contended for on the part of the Crown, and that to have a controlling interest necessitated the existence of beneficial interest in those who exercised control.

Speaking for myself, I do not find any object apparent in the Act inconsistent with that expressed in the words themselves, and, like the Master of the Rolls, I am unable to believe that the construction of the vital expression is to be ascertained by means of a meticulous search through obscurely worded portions of the Act in order to find a meaning which is not naturally apparent.

It was, however, urged that the use of the words "controlling interest" showed that there must be both control and an interest, and that a person who was merely a trustee might control but could not be said to have an interest. This contention, to my mind, lays far too great emphasis on the word "interest." I do not think one is entitled to split up the phrase and press the meaning of each portion in this way. The phrase is a composite one and the combination means no more than that the directors must have an interest such as enables them to control the activities of the company; it does not require some personal financial interest on their part which control enables them to exploit. It may be that trustees can ultimately be brought to book for activities which would not lay a beneficial owner open to attack or complaint. Nevertheless, for good or ill, the trustee, like the beneficial owner, controls, though if his powers be wrongly exercised they may in some way or other be capable of being challenged.

The Court of Appeal qualify the meaning of the phrase by excepting "bare trustee" from those having a controlling interest. As to this qualification I desire to reserve my decision. In a case such as the present, however, where the shares giving control are held by the directors not merely as trustees but also with some personal interest as well I cannot doubt that the holders have a controlling interest.

I would dismiss the appeal.

LORD SIMONDS, after stating the facts.—What constitutes a controlling interest in a company? It is the power by the exercise of voting rights to carry a resolution at a general meeting of the company. Can the directors of the respondent company by the exercise of the voting rights carry such a resolution? Yes; for they are the register

holders of more than half the ordinary shares of the company. Therefore they have a controlling interest in the company. From this result the Crown seeks an escape by the contention that shares held by a director as trustee should not be included for the purpose of computing the controlling interest. In the appellants' argument in this House and in their formal reasons this absolute veto is qualified by the suggestion that, if the director has not only the legal ownership of shares but also a predominating beneficial interest in them, they may be brought into the count.

In my opinion the Crown's contention cannot be sustained. Those who by their votes can control the company do not the less control it because they may themselves be amenable to some external control. Theirs is the control, though in the exercise of it they may be guilty of some breach of obligation, whether of conscience or of law. It is impossible (an impossibility long recognised in company law) to enter into an investigation whether the registered holder of a share is to any, and what, extent the beneficial owner. A clean cut there must be. It is for this reason that, while respectfully concurring in every other line of the judgment of the Master of the Rolls, I would reserve further consideration of that part of it which deals with the case of the so-called bare trustee. His case is not yet before your Lordships and perhaps never will be. If and when it is, the validity of the distinction made by the Master of the Rolls will have to be considered, and I should myself require a more satisfactory explanation than has yet been given of a term which, though it has statutory sanction, has never, I believe, received statutory definition.

That the meaning which I have given to the words "controlling interest" is their natural and proper meaning I have no doubt. But the great part of the argument on behalf of the Crown has been directed to showing that to some extent in regard to this very provision, but more particularly in regard to other provisions of the same Act relating to excess profits tax, the purpose of the Act will be defeated unless the beneficial interest alone is regarded and the fiduciary interest disregarded. This is a cogent argument, if two conditions are satisfied, first, that the words in dispute fairly admit an alternative construction, and, second, that the purpose of the Act can be so clearly seen that one construction will serve it and the other defeat it. Neither of these conditions is, in my opinion, satisfied. I cannot ascribe to the words "controlling interest" a meaning which would impose alike on the taxpayer and the tax collector the duty of searching out the beneficial interest behind the veil of legal forms. For it is to be observed that, if this argument is to be

effective, it is not sufficient to say that the controlling interest lies, not with the legal owner, but with the beneficial owner; the next step is to determine who, amidst all the complexities of successive interests, discretionary interests, mortgage and other interests, is for this purpose to be regarded as the beneficial owner. I must decline to admit an alternative construction which, departing from the plain and simple meaning of familiar words, requires such an unravelling. Nor is it so clear to me that, at least in respect of the provision now under review, the construction that I adopt is not consonant with what appears to be the purpose of the Act. But however this may be, and whatever may be the difficulties if this same construction is to be applied to the words in question where they occur in other parts of the Act, and particularly in paragraph 10 of the Seventh Schedule (a matter upon which I express no opinion), I cannot allow myself to be deflected by such considerations from the plain and unambiguous meaning of the provision now under review.

I agree that this appeal should be dismissed.

Appeal dismissed.

[IN THE PRIVY COUNCIL.]

BRITISH SOUTH AFRICA CO.

v.

COMMISSIONER OF INCOME-TAX.

LORD CHANCELLOR (VISCOUNT SIMON), LORD RUSSELL OF KILLOWEN, LORD MACMILLAN, LORD PORTER and LORD SIMONDS.

October 29, 1945.

INCOME-TAX—INCOME AND CAPITAL—COMPANY FORMED FOR ACQUIRING AND GRANTING MINING RIGHTS AND CONCESSIONS—GRANT OF MINING RIGHTS TO OTHER COMPANIES IN RETURN FOR FULLY PAID UP SHARES AND ANNUAL PAYMENTS FOR FIXED NUMBER OF YEARS—VALUE OF SHARES AND SUMS RECEIVED—ASSESSABILITY—INCOME OR CAPITAL—BUSINESS INCOME OR ROYALTY—COST OF ACQUISITION, WHETHER ALLOWABLE—DIFFICULTY TO APPORTION COST—PROCEDURE—COMPANY WHETHER ENTITLED TO POSTPONE ASSESSMENT UNTIL WHOLE COST WAS RECOUPED—INCOME-TAX ORDINANCE OF NORTHERN RHODESIA, 1926, Sec. 5 (a), (f).

The appellant, the British South Africa Co., was incorporated by Royal Charter in 1889, with the object, inter alia, *of carrying into effect divers concessions and agreements which had been made by certain chiefs of South Africa and such other*

concessions, agreements and grants which the company might thereafter obtain relating to mining rights in South Africa. It had special authority to carry on mining and to make concessions of mining and other rights. The company acquired numerous concessions and mining rights over various territories and gave special grants of exclusive mining rights to other companies in return for fully paid up shares in the latter and recurring annual payments in cash for a fixed number of years. The Income-tax authorities of Northern Rhodesia treated these sums as "rents, royalties, premiums and profits arising from property" falling within Section 5 (f) of the Income-tax Ordinance of Northern Rhodesia of 1926 and assessed to income-tax the full amount of the par value of the shares and the annual payments received by the appellant company under these grants without deducting the unrecouped balance of the cost of acquisition or any proportionate portion thereof:

Held, (*i*) *the sums received were the price paid upon a transfer of property and could not therefore be regarded as " rents, royalties, premiums, or any other profits arising from property " an expression which implies that the property from which the rents, royalties, premiums or other profits arise, remains in substantially the same condition in the possession of its owner and is not consistent with the property itself being transferred ;*

(*ii*) *since it was clear that the company carried on a trade and the sums in question were received in the course of that trade, it was not proper to segregate these sums from the other earnings of the company which fell to be taxed under the head " gains or profits from any trade, business, profession or vocation " mentioned in Section 5 (a) of the Income-tax Ordinance ;*

(*iii*) *the sums in question were not " capital receipts " but income derived from the business of turning into account the company's rights of winning and disposing of minerals ;*

(*iv*) *that no gain or profit could be said to arise unless and until a balance had been struck between the cost of acquisition and the proceeds of sale ;*

(*v*) *the fact that in dealing with its mineral rights the company had retained an interest in the winning of minerals either by way of a possible reverter of the property or as a shareholder in the companies to which it made grants did not make any difference for income-tax purposes, and was not a ground for disallowing the cost of acquisition in computing profits ;*

(*vi*) *the principle that where the income of a taxpayer is derived from the exhaustion of a capital asset, no deduction could be allowed*

for the cost of that asset is not applicable to cases where the article sold is that which it was the business of the assessee to acquire and to sell, and was excluded in the present case as the acquisition and realisation of mining rights was part of the company's trade;

(vii) the fact that it was impossible to allocate any part of the cost to any one or other of the individual assets or any block of such assets did not entitle the company to have the assessment of its profits postponed until the whole of the unrecouped balance of expenditure had been made good, though it might be convenient in such cases from the point of view of accountancy if the income-tax authorities chose to wait till then.

Cases referred to :—

Alianza Co., Ltd. v. Bell ([1905] 1. K. B. 184 ; ([1906] A. C. 18 ; 75 L. J. K. B. 44 ; 93 L. T. 705 ; 5 Tax Cas. 172).

Coltness Iron Co. v. Black ([1881] 6 App. Cas. 315 ; 51 L. J. Q. B. 626 ; 45 L. T. 145).

Hudson's Bay Co. v. Stevens [1905-11] (5 Tax Cas. 424).

Rhodesia Metals Ltd. v. Commissioner of Taxes ([1940] A. C. 774 ; 109 L. J. P. C. 81; 9 I. T. R. Suppl. 45).

Thew v. South West Africa Company [1925] (9 Tax Cas. 141).

Privy Council Appeal No. 65 of 1943.

T. Dourran, S. P. Hayward and *H. M. Williams*, for the appellant.

Attorney-General, C. King, R. P. Hills and *E. I. Unsworth*, for the respondent.

JUDGMENT.

VISCOUNT SIMON.—This appeal from a judgment of the Rhodesian Court of Appeal which affirmed a judgment of the High Court of Northern Rhodesia, raises the question whether certain additional assessments to income-tax made in Northern Rhodesia upon the appellant company, the British South Africa Company, for the years ending 31st March 1938, 1939 and 1940, were validly made and ought to be upheld. Inasmuch as the issue in their Lordships' opinion ultimately turns upon the nature of the business carried on by the company and of the receipts, in respect of which the assessments in question were made, a consideration of the company's history and of its transactions in relation to these receipts is necessary. The company was incorporated by Royal Charter on 29th October 1889. The Charter recites the petition by the Duke of Abercorn and others associated with him for incorporation and that the existence of a powerful British company controlled by Her Majesty's subjects in whom she had confidence and having its principal field of operations in that region of South Africa lying to the north of Bechuanaland and to the west of Portuguese East Africa would be advantageous to the commercial and other interests of Her Majesty's subjects in the United Kingdom and the Colonies and that the petitioners desired to carry into effect divers concessions and agreements which had been made by certain of the chiefs and tribes

inhabiting the said region and such other concessions, agreements, grants and treaties as the petitioners might thereafter obtain within the said region or elsewhere in Africa with the view of promoting trade, commerce, civilisation and good government as therein mentioned, and that the success of the enterprise in which the petitioners were engaged would be greatly advanced by a Royal Charter of Incorporation.

By clause 2 of the Charter the company was authorised and empowered to hold, use and retain for the purposes of the company and in the terms of the Charter the full benefit of the concessions and agreements made as aforesaid so far as they were valid, or any of them and all interests, authorities and powers comprised or referred to in the said concessions and agreements. Other clauses gave the widest administrative powers to the company and clause 24 gave it special authority (v) to carry on mining and other industries and to make concessions of mining, forestal or other rights, and (xii) to carry on any lawful commerce, trade, pursuit, business operations or dealing whatsoever in connection with the business of the company. The Charter contemplated that the objects of the company would be further defined by a Deed of Settlement. Such a deed was executed on 3rd February 1891, and it was by its third article declared that the company was formed *inter alia*: (2) to undertake and carry on the government or administration of any territories, districts or places in Africa, and therefor and therein to make laws and ordinances, and to impose and levy taxes, and raise revenue, and to establish and maintain a force of police; (3) to provide for and promote the welfare of the inhabitants of Africa, the advancement of civilization, and the development of trade; (4) to negotiate and carry into effect treaties and arrangements with any Chiefs, Rulers, Governments or Authorities (Supreme, Local or otherwise) in Africa and elsewhere; and to subsidize any such Chiefs, Rulers, Governments or Authorities; (6) to prospect explore examine and investigate countries territories places undertakings properties and claims of all kinds, and to organize conduct assist and subsidize expeditions surveys investigations experiments and testing operations of all kinds, and to collect train employ and furnish experts for any such purposes; (7) to form organize promote subsidize and assist companies syndicates partnerships institutions and associations for any purposes conducive to the interest of the company, and to hold shares in any company or corporation.

The principal concession in existence at the date of the Charter was that dated 30th October 1888, by which Lobengula, King of Matabeleland, Mashonaland and other adjoining territories granted to a

Mr. Rudd (who assigned it to, or held it on behalf of, the company) "the complete and exclusive charge over all metals and minerals situated and contained in my Kingdoms, Principalities and Dominions together with full powers to do all things that they may deem necessary to win and procure the same and to hold, collect and enjoy the profits and revenues, if any, derivable from the said metals and minerals, etc."

The territory over which these rights were granted corresponds roughly with what is now Southern Rhodesia.

Subsequently the company acquired numerous further concessions of which may be noted: (1) on 25th July 1893, the sole and exclusive right to search for, work and win precious stones and minerals in the Khamis country (now the Bechuanaland Protectorate); (2) on 25th September 1893, under documents styled "certificate of claim," the sole mining rights over certain territories in Central Africa (now in cluded in the territories of Northern Rhodesia and Nyasaland); (3) on 17th October 1900, from Lewanika, the Paramount Chief or King of the Barotse nation, the sole and exclusive right to carry on any trade and to search for, win and keep precious stones and minerals in the territory of Barotseland (now included in Northern Rhodesia); and (4) on 11th August 1909, from Lewanika the right to certain Barotseland land subject to certain conditions.

The company thus incorporated with powers of the widest range for upwards of 30 years administered at its own expense the territory now known as Southern Rhodesia and the territories north of the Zambesi river which were subsequently amalgamated and are now comprised in the Protectorate of Northern Rhodesia. In the year 1923 a great change in the character of the company took place. On 29th September of that year, it made an agreement with the then Duke of Devonshire, as Secretary of State for the Colonies, whereby it agreed to relinquish its administration of Southern Rhodesia as from 1st October 1923, and of Northern Rhodesia as from 1st April 1924. This agreement it duly carried out and thereafter became a purely trading and commercial company. Under the same agreement, which was a comprehensive settlement of matters in dispute between the Crown and the company in relation to both territories, the company received from the Crown the sum of £3,750,000, being the agreed excess of its administrative expenditure over its administration revenue in the two territories and was also recognised by the Crown as the owner of the mineral rights throughout Southern and Northern Rhodesia. The company appears throughout to have distinguished between its administration and its commercial

outgoings and receipts. It had during the same period incurred very large expenditure of a commercial character upon the acquisition, maintenance and development of its trading assets and it was a fact agreed between the parties in the proceedings, in which this appeal is brought, that "as at 30th September 1923, the unrecouped balance of the cost to the British South Africa Co. of the mineral rights, concessions, land and land rights situate in Southern Rhodesia, Northern Rhodesia, Nyasaland and Bechuanaland Protectorates belonging to the British South Africa Co. amounted to £ 5,140,383 17s. 2d."

In 1933 the company sold its mineral rights in Southern Rhodesia to the Government of that colony for £ 2,000,000 and it is a further agreed fact that as a result of the receipt of this sum and of the disposal of other assets of the company the above-mentioned unrecouped balance was reduced on 30th September 1939 to £ 924,289 15s. 5d. Before examining the specific transactions which led to the assessments now under review it will be convenient to refer to the law and practice in regard to mining rights in Northern Rhodesia. As appears from the preamble to the Mining Proclamation of 1912, it is based upon a recognition of the title of the company to the right of searching and mining for and disposing of all minerals and mineral oils in Northern Rhodesia. It is, therefore, from the company that any mining rights under the Proclamation must be derived. These are either in the form of a "Prospecting Licence" or a "Special Grant." The former is defined by the Proclamation as a "licence granted by the company to any person authorising him to acquire any mining right within the limits of this Proclamation," and in regard to the latter it is provided that "the following shall be deemed to be the special grants: (1) any mining right within the limits of this Proclamation acquired from the British South Africa Co., subsequent to the commencement of this Proclamation otherwise than by issue of or under a Prospecting Licence; (2) any mining right acquired from the British South Africa Co., within the limits of this Proclamation and before its commencement which relates to areas of greater extent than the forms of location ordinarily applicable to reef or other deposits."

It is with certain "special grants" that this appeal is concerned but it is necessary first to consider the nature of a Prospecting Licence. The common form of Prospecting Licence is annexed to the Proclamation. It is expressed to be "Available for one year only from date of issue" and to be "Not transferable" and to be issued by the company to the named licensee who agrees to the accompanying conditions. These conditions constitute the contract between the holder of the licence and the company and their importance for the present purpose

lies in this, that clause 53 of the Proclamation which deals mainly with Prospecting Licences provides that its provisions shall, except where they are inconsistent with the provisions of a Special Grant, apply to such grant and the holders thereof. The conditions provide *inter alia* (by clause 4) for the company having a paramount first charge for rents, royalties and other moneys due to it upon the licence and every mining location and interest whatsoever acquired under it and other property as therein mentioned, (by clause 6) for forfeiture in certain events, (by clause 7) for registration of the licence, (by clause 8) for the rights of the licensee for one year from the date of issue to prospect and work for minerals in Northern Rhodesia in accordance with the conditions of the licence and the provision of the mining laws for the time being in force and during the same to acquire under it and peg off one mining location. Clause 10 defines the form and extent of mining locations. Clause 14 provides that (except as therein mentioned) every registered mining location shall be held by the registered holder thereof on joint account with the company in the proportion of two-thirds by the registered holder and one-third by the company, and clause 15 that no registered mining location shall be worked for profit, except as therein mentioned, until the terms upon which such working for profit shall be permitted have been arranged with the company. Clause 16 enables the holder to submit to the company details of a scheme whereby his location may be discharged from the two preceding conditions and worked for profit. Clause 17 provides for the payment of rents and royalties by a registered holder, and clause 18 for development by him. In an annexe to the conditions the company gives notice that if satisfied upon the matters therein mentioned it will entertain proposals for the commutation of its interest in the property (that is, its one-third interest under clause 14) upon a share basis (that is, the company taking shares in a company formed to acquire the property) or upon a royalty basis.

The Proclamation repeats and gives effect to some of the contractual conditions of the Prospecting Licence and makes certain other provisions. Under section 6 the holder of a Prospecting Licence must first register his licence. By section 7 he is given in addition to the rights of prospecting for and working minerals and of pegging off a mining location thereby conferred certain ancillary rights on and over a prescribed area of land. Section 9 authorises him if he exposes or opens up a reef as therein mentioned to post a "discovery notice," and under section 10 the posting of a discovery notice confers on him for 31 days the exclusive privilege of prospecting over the area defined

in the section. Section 11 authorises him within the same period to peg off a mining location of such form and area as may be authorised by the licence and to post a "registration notice" in respect of it. Under section 13 he must apply for and obtain a certificate of registration of his mining location. By section 23 the holder of a mining location is given certain surface rights, and by section 26 he is given "so long as he is *bona fide* in pursuit of his *prima facie* rights" the right of working and extracting any of the minerals which he is entitled to win under the Prospecting Licence by virtue of which the location was acquired until such time as is mentioned in the section. Section 27 enables the holder of a mining location, if he is entitled to do so under the terms of his licence, to apply for and obtain a certificate of "special registration," and under section 28 such a certificate, subject to the provisions of the Proclamation, confers upon the holder an indefeasible title to all the surface and mining rights appertaining to such location and such a location is not thereafter to be subject to forfeiture, though the registered holder will continue to be subject to all other obligations, liabilities and provisions subject to which the location was held before the issue of the certificate. Sections 36 and 38 provide for the abandonment in certain events by the holders of unregistered and registered locations. Section 53 (dealing with special grants) has already been mentioned. Section 57 provides that so soon as a certificate of registration has been issued in respect of any special grant (for which provision is now made by the amending Ordinance VI of 1927) the provisions of the Proclamation shall mutatis mutandis and in so far as they are not inconsistent with the provisions of such grant be deemed to apply to such grant as if such grant were a mining location.

Having referred to the constitution of the company under its Charter, to certain events in its history and to the background of mining law and practice under which it operated, their Lordships must now consider the particular transactions which gave rise to the disputed assessments. These transactions fall into three groups in which three separate limited companies were concerned, (1) Loangwa Concessions (Northern Rhodesia), Ltd., which will be called "Loangwa," (2) Rhokana Corporation, Ltd., which will be called "Rhokana," and N'changa Consolidated Copper Mines, Ltd., which will be called "N'changa." It is not disputed that the agreements into which the company entered with those companies constituted "special grants" within the meaning of the Proclamation.

The transaction with Loangwa was briefly as follows: (1) By agreement of 17th May 1928, the company granted to Loangwa

exclusive right to prospect for minerals other than precious stones until 30th April 1933, and the right within that period of marking out mining claims over a prescribed area. The consideration for this grant included (a) 200,000 fully paid shares of 5s. each in Loangwa and a right to subscribe for further shares, (b) the right to an allotment of shares in such other company as was therein mentioned and to subscribe for shares in such company, and (c) the right of appointing certain directors. Under this agreement Loangwa undertook to spend certain minimum amounts varying between £60,000 and £100,000 annually in the areas comprised in the grant and were entitled to obtain further extensions of the period of the grant up to 30th April 1935. Provision was also made for payment of royalties to the company. (2) By a second agreement of 14th November 1929, the company made a special grant to Loangwa over an additional area upon substantially the same terms. (3) By a third agreement of 5th January 1933, the company extended the period of the aforesaid grants to 31st December 1940, in consideration of receiving further shares in Loangwa. (4) By a fourth agreement of 11th July 1935, the consideration payable under the preceding agreement was varied and became 50,000 fully paid shares of 5s. each. The par value of these shares was £12,500, and it is the sum of £12,500 which is item 1 of assessment disputed in this appeal.

The transaction with Rhokana was as follows: (1) By an agreement of 14th June 1928, the company granted Bwana M'kubwa Copper Mining Co., Ltd. (hereinafter called "Bwana M'kubwa") rights substantially similar to those granted to Loangwa in respect of another area for the period from 1st December 1929 to 31st December 1930, subject to a right of extension. The consideration was the payment to the company of £5,000 and in the event of the period of the grant being extended a further £5,000 annually during such extension. This agreement will be referred to as "the new M'kana grant." (2) By an agreement of 9th December 1929, the company granted to Rohkana under its then name of the Rhodesian Congo Border Concession, Ltd., rights under certain conditions to mark out mining areas in defined localities and to receive subject to the terms of the agreement special grants in respect of such mining areas and also the exclusive right to prospect for minerals from 1st January 1930 to 30th April 1935. The consideration was to be, *inter alia*, a specified proportion of shares in any companies formed to work the areas for profit and Rhokana undertook not to work the areas for profit except through a company or companies formed for the purpose. This agreement will be called "the R. C. B. grant." (3) By an agreement of 1st April 1931, between the company, Bwana M'kubwa and Rhokana the rights and obligations

under the new M'kana grant were assigned to Rhokana. (4) By an agreement of 28th August 1931, the company granted to Rhokana for the period from 6th March 1931 to 30th April 1935, the exclusive right within the area known as the Balovale area in Northern Rhodesia to prospect for minerals (other than as therein mentioned) and to mark out mining locations. This agreement will be referred to as "the Balovale grant." (5) By a further agreement of 24th February 1932, between the company and Rhokana the terms of the new M'kana, R. C. B., and Balovale grants were varied for the consideration therein mentioned. (6) By a final agreement of 20th October 1932, between the company and Rhokana expressed to be supplemental to the foregoing agreements, the period of the rights thereby conferred was extended from 30th April 1935 to 31st December 1940, subject to the spending of specified amounts on prospecting. For this extension Rhokana agreed to pay to the company the sum of £5,000 on 1st January in each of the years 1935 to 1940 inclusive. The first three of these sums of £5,000 are the second of the items of disputed assessment.

The transaction with N'changa was as follows: By an agreement of 1st September 1937, between the company, Rhokana and N'changa after recitals, whereby it appeared that Rhokana was desirous of exercising its right under the R. C. B. grant to mark out two specified mining areas, that Rhokana had agreed to assign this right to N'changa and that the company had agreed to make to N'changa a special grant of mining rights in the selected areas, Rhokana surrendered its rights under the R. C. B. grant over the areas in question and the company granted to N'changa the sole and exclusive right of searching and mining for and keeping or disposing of minerals found therein. The consideration for this grant was £2,500 fully paid shares of £1 each in N'changa to be allotted to the company. The sum of £2,500, the par value of these shares, is item 3 of the disputed assessment. These several items can now be conveniently summarised. The company received:

In respect of the year ending 30th September 1936:	
(a) 50,000 5s. shares in Loangwa at par ...	£12,500
(b) in cash from Rhokana ...	£5,000
	£17,500
In respect of the year ending 30th September 1937:	
(c) 2,500 shares of £1 each in N'changa at par ...	£2,500
(d) in cash from Rhokana ...	£5,000
	£7,500
In respect of the year ending 30th September 1938:	
(e) in cash from Rhokana ...	£5,000

On 26th March 1940, the respondent, the Commissioner of Income-tax in Northern Rhodesia, made additional assessments on the company for the years ending 31st March 1938, 1939 and 1940 in respect of the items specified above. The amounts of such assessments were the full sums of £ 17,500, £ 7,500 and £ 5,000, respectively. The Ordinance, under which the assessments were made, was the Income-tax Ordinance of Northern Rhodesia of 16th October, 1926, as from time to time amended. It is necessary to refer only to a few of its provisions. By Section 2 "chargeable income" is defined to mean the aggregate amount of the income of any person from the sources specified in Section 5 after allowing the appropriate deductions and exemptions under the Ordinance. Section 5 is the charging section and provides:

"Income-tax shall, subject to the provisions of this Ordinance, be payable at the rate or rates specified hereafter for the year of assessment commencing on 1st day of April 1928, and for each subsequent year of assessment upon the income of any person accruing in, derived from or received in the territory in respect of:

(a) gains or profits from any trade, business, profession or vocation . . .;

(c) the annual value of land and improvements thereon used by or on behalf of the owner or used rent free by the occupier for the purpose of residence or enjoyment and not for the purpose of gain or profit . . .;

(f) rents, royalties, premiums and any other profits arising from property."

Section 6 provides that tax shall be charged, levied and collected for each year of assessment upon the chargeable income of any person for the year immediately preceding the year of assessment, while Section 7 provides for special periods of assessment. Section 10 provides that for the purpose of ascertaining the chargeable income of any person there shall be deducted all outgoings and expenses wholly and exclusively incurred during the year preceding the year of assessment by such person in the production of the income. Amendments have been made to this section since the relevant date which can be disregarded. Certain other provisions of the Ordinance will be referred to later. It is now necessary to refer to the additional assessments which are in dispute. These were all made in the first place upon the footing that all the receipts in question came under Section 5 (f) of the Ordinance. They were all described in the notices of assessment as "rents, royalties, premiums and profits arising from property." To these notices objection was duly taken by the company. The grounds of objection to

the assessment in the sum of £ 17,500 for the year ending 31st March, 1938, may be taken as typical. They were (1) that neither the said sum of £17,500 nor any part thereof (whether representing cash or shares) consisted of rents, royalties, premiums or profits arising from property; (2) that neither the said sum of £17,500 nor any part thereof was income within the meaning of the Ordinance but was a gross receipt of the company's trade which so far had yielded no ascertainable profit; (3) that in any event neither the said sum of £17,500 nor any part thereof was "income accruing, derived from or received in the territory" but accrued in, was derived from and was received in the United Kingdom; (4) that the whole of the said sum of £17,500 was a capital receipt; and (5) that the said assessment was excessive in amount. The third ground of objection was not argued before their Lordships. It was rightly conceded that it was not tenable in view of their earlier decision in *Rhodesia Metals Ltd.* v. *Commissioner of Taxes* [1]. The fifth ground of objection does not appear to raise any further point. The Commissioner for Income-tax disallowed the objections and, in disallowing them, made the alternative claim (to which anticipatory objection had been raised) that the receipts in question were "alternatively gains or profits from a trade or business," thus falling within Section 5 (a) of the Ordinance. From the Commissioner's disallowance the company appealed to the High Court of Northern Rhodesia. The learned Chief Justice (Sir Charles Law, C. J.) dismissed the appeal, rejecting the contention that the receipts in question fell within Section 5 (f) of the Ordinance but upholding the alternative claim of the Commissioner that they were gains or profits from the company's trade. From this judgment the company appealed to the Rhodesian Court of Appeal, while the Commissioner cross-appealed against the judgment that the receipts in question did not fall within Section 5 (f). The Court of Appeal (Hudson, P., and Lewis and Robinson, JJ.) unanimously dismissed the company's appeal holding that the case fell within Section 5 (a) and did not find it necessary to express any final opinion upon the cross-appeal.

The company has now appealed: there has been no cross-appeal by the Commissioner but it is conceded, and the argument before their Lordships has proceeded on the footing, that it is open to him to support the assessments under either Section 5 (a) or Section 5 (f). It is convenient first to deal with the claim that the sums in question fall within Section 5 (f). Upon this point their Lordships are in agreement with the learned Chief Justice. After an examination of the several transactions he came to the conclusion that in each case the sum

(1) [1940] A. C. 774; 9 I. T. R. Suppl. 45.

received was the price paid upon a transfer of property: thus the sum of £2,500 (being the par value of the shares received from N'changa) was in his opinion "a fixed price paid on an outright transfer of certain benefits": the several sums of £5,000 in cash received from Rhokana were the consideration received upon a transfer: "the transaction was a transfer for a price, or, in other words a sale": and so also with the other items. In their Lordships' opinion, this is an accurate analysis of the transactions, and, if so, the sums received cannot be regarded as "rents, royalties, premiums or any other profits arising from property," an expression which implies that the property, from which the rents, royalties, premiums or other profits arise, remains in substantially the same condition in the possession of its owner, and is not consistent with the property itself being transferred. This is sufficient to dispose of the claim under this head but it appears to their Lordships that it fails on another ground. It may be possible —upon this question no decision is necessary—for the same receipts to fall under more than one sub-section of Section 5. But since it is clear that the company carries on a trade, the exact nature of which will presently be discussed, and the sums in question were received in the course of that trade, it does not appear a legitimate application of the section to segregate these sums from the other earnings of the company which fall to be taxed under Section 5 (a) and tax them separately under Section 5 (f).

The more difficult question arises under Section 5 (a). In the Courts of Rhodesia the argument of the company was largely influenced and directed by a fact which was agreed between the parties, *viz.*, "that it is impossible to allocate any part of such cost (*i.e.*, the sums of £5,140,383 17s. 2d. and £924,289 15s. 5d. to which reference has already been made) to any one or other of the individual assets described above (*i.e.*, the mineral rights, concessions, land, and land rights acquired by the company) or any blocks of such assets or as between the total of such assets situate in Northern Rhodesia and the total of such assets situate in all or any of the other territories." Therefore the company, while contending that there could be no gains or profits from its trade in respect of the sums in question until the cost of the assets realised had been brought into account, was faced by the fact that by its own admission the cost could not be ascertained. It therefore contended that the proper and indeed the only method by which its gains or profits could be determined was to wait until the whole of the unrecouped balance of expenditure had been made good and thereafter to assess all receipts in full. In this contention the company claimed the support of the expert evidence of

accountants that thus only could its profits be ascertained and of an arrangement made with the Inland Revenue Authorities in the United Kingdom that for the purpose of British income tax it should be thus assessed. Their Lordships can see no justification in law for this contention. It is no doubt true from the point of view of accountancy that there is no other way of finding the company's ultimate profit and equally it may be a convenient arrangement if the taxing authority chooses to adopt it. But it is impossible to find support for it in the terms of the Ordinance. The question under the Ordinance is, what is the income of the company in the particular year of assessment, and it must be answered by applying its relevant provisions as best they can be applied, not by introducing some new and supposedly more convenient method of ascertainment.

But while their Lordships cannot uphold this, the primary argument of the company, they are yet of opinion that the judgments of the Courts of Rhodesia cannot be supported. For the question still remains what is the nature of the receipts in question. The Commissioner claims that they must be brought into account as gains or profits under Section 5 (a) without any deduction, not because the cost of any particular asset is not ascertainable, but because in law no deduction is permissible, and this contention has found favour with the Courts in Northern Rhodesia, though in the judgment of Law, C. J., and to a lesser degree in the judgment of the Court of Appeal, importance is attached to the admission that cost could not be ascertained. The principles applicable to such a case as this are not in doubt.

For the purpose of assessment to income-tax (and here there appears to be no distinction between British and Northern Rhodesian tax) the proceeds of sale of an asset are brought into account if the sale is in the course of the taxpayer's trade or business. Thus if it is his trade or business to make and to sell, or to acquire and to sell, shoemaking machinery, then the proceeds of sale of such machinery are brought into account: if it is his trade to make and sell shoes and for that purpose he owns and uses shoe-making machinery, then if he sells such machinery, the proceeds of such sale are not brought into account. In the former case the machinery is sometimes called "floating" or "circulating" capital, in the latter "fixed" capital. In the former case the gain or profit arising from the sale cannot be ascertained until its cost has been ascertained: in the latter no question of cost arises, the receipts are sometimes referred to as "capital receipts" and no tax is payable. In the present case the company has contended as an alternative ground of objection to assessment that the sums in question were "capital receipts," but this contention appears to their

Lordships to be not well founded and indeed was not seriously pressed in argument. The company's substantial claim is that the receipts were in the course of its trade: it was its trade (so runs the argument) to acquire and dispose of, *inter alia*, mining rights and upon a sale or other disposition of such rights there could be no gain or profit under Section 5 (a) until the cost had been brought into account. The answer to this contention is thus stated in the judgment of Hudson, P.

"Such payments are income derived from the business of turning to account its rights under the concessions of winning and disposing of minerals by participating in the proceeds of the exploitation of such rights by its licensees: the income is therefore taxable under Section 5 (a) of the Ordinance as being the profits or gains of a trade or business and the only deductions allowable are the administrative expenses of the company," a statement which was substantially embodied in the formal reasons presented by the respondent to their Lordships' Board.

If, however, the business of the company was (as in their Lordships' opinion it was) to "turn to account" its mining rights or other property, it does not follow that the proceeds of such turning to account are chargeable to tax without any deduction for the cost of acquisition. Rather it would seem that the ordinary rule must apply and that no gain or profit can be said to arise unless and until a balance has been struck between the cost of acquisition and the proceeds of sale. Nor is it in their Lordships' opinion material that in dealing with its mineral rights the company has retained an interest either by way of a possible reverter of the property or by a shareholding in a company to which it made a special grant.

The present case finds an analogy in *Thew* v. *South West Africa Company*[1] though it is not desirable to press too closely decisions under a different taxing Act. In that case the question, which arose under the English Income Tax Act, was whether "in computing the profits arising from the trade, adventure or concern in the nature of trade carried on by the company profits derived from the sales of land ought to be taken into account." The company had been formed to acquire, purchase, and turn to account certain concessions which included rights in respect of minerals, railways and lands. Rowlatt, J., stated the question simply and decisively: "Is the article acquired for the purpose of trade?" and, coming to the conclusion that it was decided that the profits arising from its sale must be brought into account. But it is to be observed that no question was raised as to the set-off of the cost of the article. This was assumed, but the company contended that the proceeds of sale of land were "capital receipts" and need not be brought into

(1) (1925) 9 Tax Cas. 141.

account at all, as had been successfully contended in *Hudson's Bay Co.* v. *Stevens*[1].

There is however another class of case upon which the respondent relies. The learned Chief Justice had to some extent founded on the decision in *Coltness Iron Co.* v. *Black*[2], a case which arose under the English Income Tax Act then in force in relation to the profits derived from working a mine. The respondent, properly appreciating that that decision turned upon statutory provisions which had no counterpart in the Ordinance, did not press the case before their Lordships, but he urged that the true analogy is to be found in such cases, decided under the English Income Tax Acts, as *Alianza Co. Ltd.* v. *Bell*, [1905] 1 K.B. 184[3], and [1906] A.C. 18[4], which establish that where the income of a taxpayer is derived from the exhaustion of a capital asset no deduction can be allowed for the cost of that asset. Their Lordships do not wish to throw any doubt upon the validity of that principle in English law in cases to which it can be properly applied and, without deciding it, are content to assume that it may be applicable also under the income-tax law of Northern Rhodesia. But it appears to them that it is excluded as soon as the conclusion is reached that the article sold is that which it was the business of the company to acquire and to sell. So here though the mixed character of the company's objects as stated in the preamble of its Charter makes it difficult to define its trade or business, yet it appears reasonably clear that in order to effectuate its desire (to use the words of the preamble) "to carry into effect divers concessions and agreements...and such other concessions, agreements, grants and treaties as the petitioners may hereafter obtain" the acquisition and realisation of mining rights must take a leading place.

If this conclusion is reached, it becomes, as has already been pointed out, immaterial what method is adopted by the company for the development and realisation of its asset. In his elaborate and careful judgment in the Court of Appeal the learned President lays great stress on the fact that the company in effect "participated in the results of the winning of minerals by prospectors," and it is this consideration that leads him to the conclusion that against the profits derived from such participation no allowance for cost can be made. The relevant transactions have already been stated in sufficient detail: they are in their Lordships' opinion in substance indistinguishable from outright sales of mining rights. But even if they are to be distinguished by the fact that the company remains interested as a shareholder in other companies in the winning of minerals, this is not a

(1) (1905-11) 5 Tax Cas. 424.
(2) (1881) 6 App. Cas. 315.
(3) [1905] 5 Tax Cas. 60.
(4) *Alianza Co. Ltd.* v. *Bell* [1906] 5 Tax Cas. 172.

difference which affects the position for income-tax purposes. The company is still realising in the way that appears most advantageous the asset which it is its business to acquire and realise. It is to be observed that, if the company itself embarked on mining operations, different considerations would arise. It would then be subject to and entitled to the benefits of the provisions of Section 11 (2) of the Ordinance and its amendments.

Their Lordships are of opinion, therefore, that the judgment of the Court of Appeal cannot stand as it is. The question remains, what is the proper course now to be taken? It was agreed by counsel upon the hearing of this appeal that the figures, upon which the additional assessments now under review were based, appeared in the returns made by the company. It is provided by Section 40 (2) of the Ordinance that: "where a person has delivered a return the Commissioner may (a) accept the return and make an assessment accordingly; or (b) refuse to accept the return and to the best of his judgment determine the amount of the chargeable income of the person and assess him accordingly."

The Commissioner acting presumably under this sub-section and under Section 41 of the Ordinance has made the disputed additional assessments. In doing so he has exercised his judgment on a wrong principle, for he has assumed that the receipts in question are chargeable without deduction. The company has in their Lordships' opinion, discharged the onus which lies upon it of proving that the assessments are excessive, for it is clear that some deduction should be allowed. In the circumstances it appears to their Lordships to be the proper course to refer the matter back to the Commissioner for re-assessment "to the best of his judgment." An opportunity will thus be given to the company to submit such considerations in regard to deductions in respect of these particular receipts as appear to them relevant and reasonable and to the Commissioner, having weighed them, to make a re-assessment upon the proper basis at what he judges to be the appropriate figure. The Commissioner must pay the costs of the company of this appeal and in the Courts of Northern Rhodesia.

Order accordingly.

[IN THE HOUSE OF LORDS.]

LEVER BROS. AND UNILEVER, LTD.

v.

INLAND REVENUE COMMISSIONERS.

VISCOUNT SIMON, LORD THANKERTON, LORD WRIGHT, LORD PORTER, LORD UTHWATT.

February 5, 7, 8, March 22, 1946.

EXCESS PROFITS TAX—CAPITAL EMPLOYED IN TRADE OF COMPANY—LARGE SUMS PAID BY COMPANY INTO FUND CREATED TO PROVIDE PENSIONS

FOR EMPLOYEES—WHETHER THAT A REDUCTION OF CAPITAL WITHIN MEANING OF SECTION 14 (2) AND PART II OF SCHEDULE VII OF FINANCE (No. 2) ACT, 1939.

In 1922 a fund was created by a trust deed to provide pensions for the employees of the appellant company, their widows and dependants, the contributions of the employees and employers being fixed so as to make the fund self-supporting. In 1937 the appellant decided to increase the provision for widows of employees and that the appellant should pay into the fund an annual contribution actually sufficient to provide for the increase. In 1939, accordingly, a sum of £ 18,993 was paid to the fund, and in 1940 the appellant paid in £ 131,196 to commute the prospective annual contributions for increased widows' pensions. Also in 1940 £ 895,329 was paid into the fund to enable pensions to be equalised as between employees of the different companies then amalgamated under the appellant. The question was whether, by making these two lump sum payments the appellant had pro tanto *reduced its capital employed in its trade or business, within the meaning of Section 14 (2) and Part II of the Seventh Schedule of the Finance (No. 2) Act, 1939, or whether it had acquired thereby something equivalent which left its total capital unaffected by these operations. The appellant alleged that the asset gained was a contented staff, and by these payments acquired a contractual right to compel the trustees of the fund to make the increased payments and that right was an asset. The Commissioners found that there was no contract between the trustees and the appellant in the deed of trust:*

Held, *that the deed of trust provided how the trustees were to administer the trust, but that did not constitute a contractual relation to be enforced by the settlor by action for an injunction or otherwise, and, even if a resulting trust could emerge, no Court would grant an application by the appellant for an order for the administration of the fund based on the allegation that it had a real interest. The result was that the appellant had parted with these sums and thereby had lost capital which was not replaced by new capital employed in its trade or business.*

Decision of the COURT OF APPEAL (171 L. T. 203) *affirmed.*

Cases referred to:

British Insulated and Helsby Cables, Ltd. *v.* Atherton [1925] (95 L.J.K.B. 336 ; [1926] A.C. 205 ; 10 Tax Cas. 155).

Inland Revenue Commissioners *v.* Byron Ltd. [1943] (170 L.T. 415 ; 60 T.L.R. 367 ; affirmed in House of Lords [1945] 114 L.J.K.B. 345 ; 14 I.T.R. Suppl. 1).

Appeal from the judgment of the Court of Appeal.

The material facts are stated in the headnote.

Tucker, K.C., and *F. Heyworth Talbot*, for the appellant.

Sir Patrick Hastings, K.C., *J. H. Stamp* and *Reginald Hills*, for the respondent Commissioners.

The arguments appear in the judgment of Viscount Simon.

VISCOUNT SIMON.—The question in this appeal is whether, when computing the capital of the appellant for purposes of excess profits tax for the chargeable accounting period January 1 to December 31, 1940, two sums of £131,196 and £895,329 paid in that year by the appellant and its subsidiary companies to the trustees of a fund called the Union Superannuation Fund (hereinafter called the fund) should be deducted, as the Crown contends; or whether, as the appellant argues, there should be no deduction, as the appellant by making such payments acquired something to be reckoned as part of its capital of equal amount.

The Commissioners, for the special purposes of the Income Tax Acts, decided in favour of the Crown, and stated a case for the opinion of the High Court. Macnaghten, J., allowed the appeal, holding that "by the payments in question the appellant did acquire the right, as against the trustees of the fund, to compel them to pay the increased benefits to its employees" and that it acquired an asset equivalent to the payments made. The Court of Appeal (Lord Greene, M. R., Finlay, L. J., and Morton, L.J.) remitted the case to the Special Commissioners to hear the parties further and to reach further findings on questions formulated by the Court. On receiving the Commissioners' answers in a supplemental case, the Court of Appeal reversed the decision of Macnaghten, J., and decided in favour of the Revenue, while giving the appellant leave to appeal to this House.

The origin of the fund was a trust deed made in 1922 by Van den Berghs, Ltd., for the provision of superannuation allowances and pensions for its employees, their widows and other dependants, the fund being contributory and the contributions of employees and employers being fixed so as to make the fund self-supporting. There is a long history, set out in the case, in the course of which the benefits of the fund were made available to employees of other companies whose enterprises and interests became consolidated and were ultimately acquired by the appellant, but for the purpose of this appeal it is enough to say that in 1937 the appellant decided that the provision for widows of employees should be increased from January 1, 1938, and it was arranged, as stated in a circular letter of July 1, 1937, that the appellant would pay into the fund an annual contribution actuarially sufficient to provide for this increase. The appropriate amounts were duly paid into the fund for the years 1938 and 1939, the amount in the latter year being £18,993. Later in 1939 the appellant arranged with the trustees to commute the prospective annual contributions for increased widows' pensions. Upon an actuarial valuation it was agreed with the trustees that the commuted value was £131,196, and the appellant in 1940 paid this sum into the fund. It is the effect of this payment upon

the computation of the appellant's capital which is the first question to be decided.

The other amount, £895,329, was paid into the fund in the same year in order to enable pensions to be equalised as between employees of the different companies now amalgamated under the appellant. Previously, the appellant had been accustomed to supplement pensions paid from the fund to late entrants by itself making a further payment, but in 1939 the appellant decided to arrange that, in the case of certain classes of employees, the supplement should be paid from the fund. The additional amount paid in, by arrangement with the trustees, was actuarially calculated to represent this further burden on the fund.

The question therefore emerges whether, by making these two lump-sum payments, the appellant has *pro tanto* reduced its capital employed in its trade or business, within the meaning of Section 14 (2) and Part II of the Seventh Schedule of the Finance (No. 2) Act, 1939, or whether it has acquired thereby something equivalent which leaves its total capital unaffected by these operations.

At one time it was suggested that the asset acquired was an assurance of enhanced loyalty and contentment of the appellant's staff, and Macnaghten, J., in rejecting the idea that "the appellant got nothing for its money", later observed that "in common parlance, the transaction was a purchase of benefits by way of allowances and pensions for its employees, their widows and dependants; and thereby to make them more content with their employment or, at least, to remove a cause of discontent."

The question, however, is not whether the appellant got nothing for its money but whether the results attained constitute "capital." Appellant's counsel, in his able argument before us, repudiated the contention that the asset gained was a contented staff, and rightly so, not only because such a gain cannot be evaluated as capital, but because what enters into the computation of capital for this purpose is defined in the statute, and is (as was observed in the recent case of *Inland Revenue Commissioners* v. *Byron* [1]) limited to that.

The two grounds on which it was sought to establish the appellant's claim are (1) that the appellant by these payments acquired a contractual right to compel the trustees of the fund to make these increased payments, and that this right is an asset to be valued at the price at which it was acquired; (2) that, in certain highly problematical events, there might arise a resulting trust in favour of the appellant, and that this circumstance would give to the appellant the *locus standi* of being able to enforce the due administration of the trust. According to the appellant, this would either be an "asset acquired otherwise than by purchase" or, if not an asset, an advantage which could be included in the computation of capital. I do not

(1) [1946] 14 I.T.R. Suppl. 1.

think that any such advantage, if not covered by the word " assets " in the Schedule, can be so included.

Be that as it may, the answers given by the Court of Appeal to these two arguments appear to me to be irresistible. As for (1) the Commissioners in the supplemental case find that there was no contract between the trustees and the appellant in the deed of trust. They are both parties to the deed, and the document, as one would expect, provides how the trustees are to administer the trust. Nevertheless, this does not constitute a contractual relation, to be enforced by the settlor by action for an injunction or otherwise. I accept the view laid down by the Master of the Rolls when he says: "It is not the case, where a person sets up a trust under a document between himself and trustees, in which the trustees undertake to execute the trust according to the terms laid down, that he obtains against the trustees a contractual right to compel them to enforce the trust. The provisions of the trust, as laid down in such a document, merely constitute the charter under which the trustees undertake to operate for the benefit of the beneficiaries; but that undertaking is not an undertaking towards the settlor; once he has constituted the trust he is no longer concerned with it. The trustees' obligations then are obligations towards the beneficiaries, and it is the beneficiaries alone who can enforce them."

As for (2), even if a resulting trust could emerge in certain events very difficult to conceive as occurring, it is " of such a remote nature and so unlikely ever to produce any concrete result, " as Lord Greene says, that no Court would listen to an application by the appellant for an order for the administration of the fund based on the allegation that it had a real interest. The suggested resulting trust does not, in the circumstances, confer a right to interfere. If the appellant so desired, it could remove unsatisfactory trustees and substitute new ones to its liking, even members of its own board of directors.

The conclusion is that the appellant has parted with these sums for good and sufficient reasons, but with the result that it has lost capital which is not replaced by new "capital employed in its trade or business."

The appellant sought to found an argument on the well-known observation of Lord Cave in *British Insulated and Helsby Cables, Ltd.* v. *Atherton*[1], that a test of capital as against income may be found by asking whether expenditure is incurred for the purpose of securing " an advantage of enduring benefit." But that is a test for the purpose of determining what expenditure may be set against receipts for the assessment of profits under Case I of Schedule D. It has nothing whatever to do with the definition of capital in connection with excess profits tax.

I move that the appeal be dismissed with costs.

(1) [1926] A.C. 205; 10 Tax Cas. 185.

LORD THANKERTON.—I have had the privilege of considering the opinion which has just been delivered by my noble and learned friend, and I desire to express my agreement with it. I would only add a few observations. The appellant's first contention based on an alleged contractual right appeared to me to be purely academic, in view of the Commissioners' finding of fact in paragraph 3 (*d*) of the supplemental case that, if there was such a right, no monetary value could be attached to it so as to be included in computing the capital. The same finding applied to the monetary valuation of a resulting trust, if such a right existed. But, before this House, the appellant maintained that the asset obtained in return for the payments in question was not the value of the resulting trust, but the value of the legal right to enforce the carrying out of the trust purposes, which accrued to it as the result of the resulting trust. It will be noted that the findings of the Commissioners in paragraph 3 (*b*) are of no avail to the appellant in this contention, for the question and answer both assume the absence of a resulting trust, and, moreover, the answer attributes the monetary value stated, not to any right to enforce the trust, but to the relief "not merely from what was recognised or felt in general to be an obligation, but from the prospective yearly contribution of certain sums." The appellant did not maintain this view.

As to the contention that there was a resulting trust, in virtue of which the appellant obtained a right to enforce the trust, which constituted capital within the meaning of the material statutory provisions, I have nothing to add to the opinion of my noble and learned friend and the opinion of the learned Master of the Rolls.

LORD WRIGHT.—My Lords, I agree that this appeal should be dismissed for the reasons explained by my noble and learned friend, Viscount Simon, in which I completely concur.

LORD PORTER.—I also concur.

LORD UTHWATT.—I agree.

Appeal dismissed.

[IN THE COURT OF APPEAL.]

DICKINSON & CO. *v.* BRISTOW.

LORD GREENE, M. R., SOMERVELL, L. J., COHEN, L. J.

February 19, 1946.

BAD DEBT—RECOVERY OF PART OF DEBT WHICH HAD BEEN WRITTEN OFF—ORIGINALLY DEBT ENTERED IN COMPANY'S ACCOUNTS AS TRADING RECEIPT—SUBSEQUENT ALLOWANCE BY REVENUE OF AMOUNT OF DEBT AS TRADING LOSS BY REASON OF HAVING BEEN WRITTEN OFF—SUBSEQUENT

RECEIPT OF PART OF DEBT TO BE ENTERED AS TRADING RECEIPT—INCOME TAX ACT, 1918 (8 & 9 GEO. 5, c. 40), SCHEDULE D, RULES APPLICABLE TO CASES I AND II, RULE (3) (*i*).

A debt owed to a company was brought into its accounts for a particular year as a receipt in accordance with rule 3 (i) of the rules applicable to Cases I and II of Schedule D. In subsequent years the debt was written off as a bad debt, and was allowed as a deduction under the same paragraph of the rule. Subsequently the company received certain moneys in respect of part of the debt:—Held, *that the moneys thus received should be entered as receipts in the company's accounts for the purposes of income tax, in spite of the fact that the company had already brought the amount of the debt as a receipt into its accounts in a former year. The writing off of the debt and the consequent allowance in respect of the writing off had had the effect of reversing the position that had been established by entering the debt as a receipt in the accounts.*

The dicta of the majority of the House of Lords in ABSALOM v. TALBOT [1944] (113 L.J.K.B. 369; [1944] A.C. 204) *that the amount of a bad debt could be deducted under the rule, no matter at what time it became a bad debt, followed in preference to the dicta of the Privy Council in* GLEANER CO. v. ASSESSMENT COMMITTEE [1922] (91 L.J.P.C. 181; [1922] 2 A.C. 169) *that in order to justify the allowance of a bad debt as a deduction, the debt had to be a bad debt on the occasion when it was first brought into the accounts.*

Cases referred to:—

Absalom v. Talbot [1944] (113 L.J.K.B. 369; [1944] A.C. 204).

Anderton & Halstead, Ltd. v. Birrell [1931] (101 L.J.K.B. 219; [1932] 1 K.B. 271; 16 Tax Cas. 200).

Gleaner Co. v. Assessment Committee [1922] (91 L.J.P.C. 181; [1922] 2 A.C. 169).

Appeal from the judgment of Macnaghten, J.

This was an appeal by William Dickinson & Co. from the judgment of Macnaghten, J., allowing the appeal of the Crown from the decision of the General Commissioners for Newcastle-on-Tyne. Between December, 1935, and June, 1936, the company's Spanish customers, to whom it had been exporting coal, became indebted to the company in the aggregate sum of £10,716, and in accordance with the usual practice, in pursuance of rule 3 (*i*) of the Rules applicable to Cases I and II of Schedule D, this debt was included at its full value as a trading receipt in the accounts of the company for the purposes of income tax for the year ending April 5, 1936. As the result of the civil war in Spain, by the year 1938 the whole of this debt became a bad debt, and the directors wrote off part of the debt in 1937 and the remaining part of it in 1938. The sums so written off were allowed as trading losses for the respective years 1937-1938 and 1938-1939 in accordance with a long established practice of the Board of Inland Revenue. As

the result of an advance made by the British Government in 1940 of £2,000,000 to the Spanish Government for the purpose of facilitating the payment of debts due by Spanish nationals to traders in the United Kingdom, the company recovered £5,115 9s. 6d. in the year ending March 31, 1941, and £333 3s. 11d. in the year ending March 31, 1942, in respect of the Spanish debt owing to it. The Inspector of Taxes claimed that both such sums should be included as trading receipts for the purposes of income tax for the respective years in which they had been received. The General Commissioners decided that these sums should not be so included. Macnaghten, J., held that they should be so included, and he therefore reversed the decision of the Commissioners. The company appealed.

Grant, K.C., and *Charlesworth*, for the appellant company.

The Solicitor-General (Sir Frank Soskice, K.C.) and *R. P. Hills*, for the respondent, the Inspector of Taxes.

LORD GREENE, M.R.—The point raised by this appeal is one which might fairly be described as singularly devoid of merit. We have to decide a bare question of law.

Put in diagrammatic form, so to speak, the question may be thus formulated. A trading company in the year 1 sells goods on credit. The amount so owing to it is brought into account in the computation of its profits and gains for the year 1. In the years 2 and 3 events happen which, first of all, depreciate the value of that debt, and later on destroy its value altogether. In the accounts for the years 2 and 3 the Revenue accept the view that the depreciation and final devaluation of the debt should be made the subject of an allowance in those respective years. In the year 4 further events happen of a quite unusual and, indeed, unexpected nature, which have the effect of converting the debt which has been treated as bad into a perfectly good debt, which is paid in the year 4. The Revenue then says: "In taking the account of your profits and gains for the year 4, you must bring in that sum as a receipt. You have received it in the year 4, and you must accordingly bring it into account". It is not a question of revising or amending, by additional assessment or otherwise, any of the assessments for the years 1, 2 or 3. The claim of the Revenue is to treat that receipt as a receipt of income for the year 4.

The only statutory provision which bears on this question to which I need refer is rule 3 (*i*) of the Rules applicable to Cases I and II of Schedule D to the Income Tax Act, 1918. That sub-rule is as follows: "In computing the amount of the profits or gains to be charged, no sum shall be deducted in respect of . . . any debts, except bad debts proved to be such to the satisfaction of the Commissioners and doubtful debts to the extent that they are respectively estimated to be bad". Then there is a provision as to bankruptcy or insolvency: "In the case of the bankruptcy

or insolvency of a debtor, the amount which may reasonably be expected to be received on any such debt shall be deemed to be the value thereof."

There is one curious point about that provision which I only note in passing. It finds its place in a series of sub-rules, all of which appear to deal with deductions, such as disbursements, expenses or losses, whereas this particular sub-rule prohibits the deduction of any debts. A debt would obviously only be the subject of deduction if the taxpayer was entitled to say to the Revenue: "Although I keep my profit and loss account on the basis of treating debts as being equivalent to receipts, yet, as between me and the Revenue, I am entitled to deduct debts because I have not yet been paid." The effect of the rule is to treat the account, which has to be taken for income tax purposes, on the same basis as a commercial account, and to prohibit the deduction of debts on the ground that they still remain to be paid and consequently ought to be brought into account in the year in which they are paid. The practice always has been, and rightly, having regard to that language, to treat debts in the ordinary commercial way as though they were receipts of the year and bring them into the account accordingly.

The first question which falls to be decided in examining this matter is one on the true construction of that sub-rule. In the case of the *Gleaner Co.* v. *Assessment Committee* [1], a case in the Privy Council on appeal from Jamaica arising out of the Jamaica Income Tax law, it is said that a provision similar in terms to this one did not justify the giving of an allowance in respect of doubtful or bad debts save on the occasion when the debt was first brought into the account. For instance, the reasoning of that decision, if it applied to the present case, would have produced this result, that the allowances granted by the Revenue in years 2 and 3 would not have been authorised by the language of this sub-rule. The allowances could only have been made in respect of the debt in the year 1. In the year 1 there was no ground at all for writing it down, much less for treating it as altogether bad, and, therefore, nothing fell to be done about it. The consequence would have been, if that view applied, that the allowances granted by the Revenue in the years 2 and 3 would have been merely voluntary allowances not made pursuant to any provision of the statute. It was further said in that case that: "If, therefore, debts decided to be doubtful in one year were found to be good at a later date, apart from the provisions of Section 30"—that is, of the Jamaica Act—"there are no means whatever of obtaining further income tax upon the amount, nor, if their value further diminish, could they be the subject of reassessment." That language, if it were applicable to the present case, would preclude the Crown from maintaining the claim it now makes, namely, to have the receipt in the year 4

(1) [1922] 2 A.C. 169 ; 91 L.J.P.C. 181.

brought into account in respect of that year. But in the recent case of *Absalom* v. *Talbot* [1], in the House of Lords, the effect of sub-rule (*i*) was considered in that connection. It is right to say that the observations to which I am about to refer were by way of *dicta* only. But of the five noble and learned Lords who were sitting on that appeal, three, namely, the Lord Chancellor (Lord Simon), Lord Atkin and Lord Porter, emphatically and clearly dissented from the view which had been expressed by the Privy Council in the *Gleaner case*, and held—I repeat by way of *dictum* only—that it was legitimate for the Revenue to make allowance in a subsequent year in respect of a debt which in the earlier year had been treated as a perfectly good debt. The other two noble and learned Lords, Lord Thankerton and Lord Russell of Killowen, appear to have been inclined to take the opposite view, although they did not express any concluded opinion. We have, therefore, three clearly expressed statements in that case as to the true construction of this sub-rule. We are not bound, of course, to follow them I think it falls to us to decide whether, in our opinion, those expressed opinions are in accordance with the true meaning of the sub-rule. If we came to the conclusion that they were not, and that the view of the Privy Council in the *Gleaner case* was preferable, the result of this case might well have been different to what I consider it should be, because then the allowances would have been purely *ex gratia* allowances. But, in my opinion, the views expressed by those three members of the House in *Absalom* v. *Talbot* [1] are correct.

I think I am right in saying that no one of the three noble and learned Lords thought it necessary to examine carefully the language of the sub-rule in order to show how and why the construction of it admitted the making of such allowances as we have to consider in this case. But it seems to me that that task is not really a difficult one, for this reason. When one looks at the language, it starts, first of all, by prohibiting a deduction in respect of a debt. That would appear to mean, as I have said, that a taxpayer cannot come and say: "Exclude this debt from the computation because it has not yet been paid." But in this case, in the years 2 and 3 the company was in effect saying to the Revenue: "We claim a deduction in those two years in respect of this debt; the reason being that in those years 2 and 3 something has happened to it which has had the result, first, of reducing it in value, and subsequently destroying the value altogether, on the ground that it was bad." The company claming to make that reduction in respect of the debt in the years 2 and 3 is entitled to the relief which the sub-rule allows, namely, that, if it is a bad or doubtful debt proved to be such to the satisfaction of the Commissioners, a deduction may be made. That is exactly what happened.

(1) [1944] A.C. 204; 113 L.J.K.B. 369.

The contrary view, of course, is that the only occasion when the question of badness or doubtfulness of debts falls to be considered is the occasion when the debtor is bringing his debt into the account. But I cannot see that the language of this sub-rule necessarily leads to that result. It applies to any deduction claimed in respect of any debt, at any time in the year it seems to me, and such a claim was precisely the claim that was made by the company in this case. I am accordingly of opinion that we ought to follow the *dicta* of the majority of the House in *Absalom* v. *Talbot*[1]. That is the first question to be considered.

The next question is: What is to be done where, in a subsequent year the debt having in the meanwhile become a good debt, is paid? In the *Gleaner case*, as I have said, it was regarded as a consequence of the early part of the decision, that a receipt in a subsequent year of a debt previously treated as bad could not be treated as something to be brought into account in that year, or as a ground for revising or reopening the earlier assessments. In the *Absalom case* that consequence was not referred to, save by Lord Porter. He said this (113 L.J.K.B., at p. 380; [1944] A.C., at p. 226): "Your Lordships' attention, however, has been drawn to the practice in the past of the Inland Revenue authorities of making an allowance in respect of losses for bad or doubtful debts as and when they occur, though the debt itself was originally treated as being of its face value in a previous year's accounts. Such a practice necessitates, I think, the corresponding obligation on the part of the taxpayer to submit in a later year to an increase in the sum at which a debt previously treated as bad or doubtful should be brought into account if in fact a payment greater than the assumed value had been obtained or seems likely to be obtained, on a later occasion." That appears to mean that, in Lord Porter's view, a subsequent improvement in the debt in a later year could be given effect to, notwithstanding that the debt had not in fact been paid because he uses the phrase "seems likely to be obtained." I am not sure that I would accept that view, but we have not to consider it here because we are now dealing with a case where the debt has in fact been paid. Then he refers to *Anderton & Halstead, Ltd.* v. *Birrell.* He says (113 L.J.K.B., at p. 380; [1944] A.C., at p. 227): "The decision in that case turned upon a different point, namely, whether the debt could be treated as having been mistakenly valued at too low a figure in the years in which the value had been written down, so that the profits of those years could be recalculated, the value written up, and the sum, on which tax was payable, increased." That was a demand by the Crown to get what it wanted by a different method, namely, by reopening the earlier assessment. Lord Porter goes on: "The argument that it could be so treated was held to be unsound, but nothing was said to throw doubt upon the right of the subject to have the value of

(1) [1944] A.C. 204; 113 L.J.K.B. 369.

a debt reduced at any time as and when it was discovered to be bad or doubtful, or of the Crown to have it increased in some future year if it proved to be of greater value than had been assumed in an earlier year when it was brought into account or valued." Lord Porter took the view that, if the debt was paid in the subsequent year in whole or in part, that payment was a matter to be brought into account; but he also seems to have taken the rather more extreme view that, even if it were not paid, a mere change of its value would justify giving effect to that change in the account of the year in which it took place. As I have said, I am not prepared, without further consideration, to accept that.

If one looks at the position when the company in the year 4 received this sum, the first question that occurs to one is to ask this: As between the Revenue and the taxpayer, has the sum so received in any shape or form been brought into account for tax purposes? Counsel for the appellant says: "Yes, it has. It was brought into account in the form of a debt in the year 1, according to the ordinary practice, and, having been brought into account in the form of a debt in the year 1, it is not possible to strike it with tax in the year 4 when it is received." The reason why a receipt is not taxed in the year of receipt, I apprehend, is that it has already been taxed in the form of a debt in the year to which the debt is referable. But, in the present case, it seems to me impossible to disregard what has happened in the years 2 and 3 as affecting the position of the taxpayer on the one hand and the Crown on the other in respect of this particular receipt. It seems to me, looking at the whole of what has happened, that it is quite impossible to say that this receipt ought to be treated as having been previously brought into account for tax at all. It is perfectly true that it was originally brought into account in its then shape of a debt, but the effect of what happened in years 2 and 3 appears to me to have reversed that position altogether. The net result is that, at the end of the year 3, it is untrue to say that this particular item has been brought into account for tax purposes because, although it was brought in in calculating the profits in the year 1, it was taken out again in calculating the profits of the years 2 and 3. Here is a receipt in year 4. Why should not it be struck with tax when it has not so far been brought into effective computation? It is not like an ordinary trading debt which, when it is received, would not be taxed a second time. This is a peculiar debt, having regard to its history, of which it is impossible to say that, at the time when it was received, it had been brought into account for tax purposes while it was still only a debt. You cannot put what happened in the year 1 into a sort of watertight compartment and disregard what happened in the years 2 and 3. In my opinion, you must look to the result of all the transactions and ask yourself in the year 4: What is the status of this receipt as between the taxpayer and the

Revenue? Is it a receipt which must be excluded from computation on the ground that it has already come in in another form, namely, the form of a debt, or is it to be treated as something which has never been brought into account at all owing to the particular provisions of sub-rule 3 (*i*), and to what, in fact, was done under those provisions? In my opinion, the Crown's contention is right in this matter.

Counsel for the appellant pointed out that the receipt in the year 4 had its origin, from the commercial point of view, in the coal contract made in the year 1. No doubt that is perfectly true, but the question we have to decide is: What is the status of this receipt as between the taxpayer and the Revenue, having regard to the events which have happened? Clearly, as he points out, if in year 1 there had been a debt which for some reason had been omitted and then in year 4 the amount of that debt was paid, the proper course, according to the ordinary practice, would be not to treat that as a trading receipt of year 4 but as a trading receipt of year 1, when it ought to have appeared in the accounts in its then form of a debt. That is perfectly true, but the proper remedy in that case is to reopen, by proper procedure, the account of year 1. But that is not this case at all. That is a case of mere omission. This is a case where the whole position of the debt has been completely revolutionised by what happened in years 2 and 3. I can see no reason for saying that, as between the taxpayer and the Revenue, this receipt must be attributed to the year 1.

In my opinion, the learned Judge, who took that view contrary to the view of the Commissioners, was perfectly right, and the appeal must be dismissed.

SOMERVELL, L.J.—I agree.

COHEN, L.J.—I also agree.

Appeal dismissed.

Leave granted to appeal to the House of Lords.

[IN THE HOUSE OF LORDS.]

PONTYPRIDD AND RHONDDA JOINT WATER BOARD

v.

OSTIME (H. M. INSPECTOR OF TAXES).

VISCOUNT SIMON, LORD THANKERTON, LORD WRIGHT, LORD PORTER, LORD SIMONDS.

January 25, 28, 29; March 29, 1946.

INCOME TAX—PROFITS OR GAINS OF BUSINESS—SUBSIDIES FROM PUBLIC FUNDS—SUMS PAID UNDER PRECEPT TO WATER BOARD BY DISTRICT COUNCILS—WHETHER TRADE RECEIPTS.

The appellant board were assessed under Case I of Schedule D of the Income Tax Act, 1918, in the estimated sum of £10,000 for the year 1939-1940 in respect of the profits of its trade, which was that of an undertaking for the supply of water. Certain sums had been paid, under precept, to the appellant board by the Pontypridd and the Rhondda District Councils under Section 91 of the Pontypridd and Rhondda Water Act, 1910, and the question was whether those sums fell to be included as receipts in the computation of the appellant board's trade profits. The sums so received under precept were to meet an estimated deficiency in the result of what were admittedly trading activities :—Held, *that under the decision of this House in* LINCOLNSHIRE SUGAR CO. *v.* SMART [1937] (106 L.J.K.B. 185; [1937] A.C. 697; 20 Tax Cas. 643) *payments in the nature of a subsidy from public funds made to an undertaker to assist in carrying on his business were trading receipts to be brought into account in arriving at the profits or gains under Case I of Schedule D, and the appellant board were not within the exception to that proposition; that if the undertaker was a rating authority, and the subsidy was the proceeds of rates imposed by it, or came from a fund belonging to the authority, the identity of the source with the recipient prevented any question of profits arising* (FORTH CONSERVANCY BOARD *v.* INLAND REVENUE COMMISSIONERS [1931] (100 L.J.P.C. 193; [1931] A.C. 540; 16 Tax Cas. 103)) *as the precepts which the appellant board issued called for lump sums to be contributed by the two urban district councils, which they might pay either from their respective district funds or by levying rates. They were not agents for the appellant board in finding the money, but distinct parties. There was therefore no such identity between contributors and recipients as removed the board from the application of the first proposition set out above, and the sums so received were received as sums which went to make up the profits or gains of their trade.*

Decision of the COURT OF APPEAL (60 T.L.R. 552) *affirmed.*

Cases referred to :—

Attorney-General *v.* Black [1871] (40 L.J.Ex. 194 ; L.R. 6 Ex. 308 ; 1 Tax Cas. 52).

Attorney-General *v.* Scott [1874] (28 L.T. 302 ; 1 Tax Cas. 55).

Forth Conservancy Board *v.* Inland Revenue Commissioners [1931] (100 L.J.P.C. 193 ; [1931] A.C. 540 ; 16 Tax Cas. 103).

Glasgow Water Commissioners *v.* Inland Revenue Commissioners [1875] (2 R. 708 ; 1 Tax Cas. 28).

Glasgow Water Commissioners *v.* Miller [1886] (13 R. 489 ; 2 Tax Cas. 131).

Lincolnshire Sugar Co. *v.* Smart [1937] (106 L.J.K.B. 185 ; [1937] A.C. 697 ; 20 Tax Cas. 643).

Mersey Docks and Harbour Board *v.* Lucas [1883] (53 L.J.Q.B. 4 ; 8 App. Cas. 891 ; 2 Tax Cas. 25).

Municipal Mutual Insurance, Ltd. *v.* Hills [1932] (147 L.T. 62 ; 16 Tax Cas. 430).

Seaham Harbour Dock Co. *v.* Crook [1931] (16 Tax Cas. 333 ; 48 T.L.R. 91).

Appeal from the judgment of the Court of Appeal.

The essential facts are stated in the headnote.

Tucker, K. C., and *Donovan, K. C.*, for the appellant board.

Sir Patrick Hastings, K. C., and *Reginald P. Hills*, for the respondent Inspector of Taxes.

The arguments sufficiently appear from the judgment of Lord Thankerton.

Their Lordships took time for consideration.

VISCOUNT SIMON.—I have had the advantage of considering the opinion which my noble and learned friend Lord Thankerton is about to deliver, in which he has fully set out the facts in this case, and has examined and analysed the authorities. I agree with his conclusion and will limit myself to a brief statement of two contrasted propositions; the real question in the appeal seems to me to be under which of these two propositions the present case falls.

The first proposition is that, subject to the exception hereafter mentioned, payments in the nature of a subsidy from public funds made to an undertaker to assist in carrying on the undertaker's trade or business are trading receipts, that is, are to be brought into account in arriving at the balance of profits or gains under Case I of Schedule D. It is sufficient to cite the decision of this House in the sugar-beet case (*Lincolnshire Sugar Co.* v. *Smart*[1]) as an illustration.

The second proposition constitutes an exception. If the undertaker is a rating authority and the subsidy is the proceeds of rates imposed by it or comes from a fund belonging to the authority, the identity of the source with the recipient prevents any question of profits arising; see, for example, Lord Buckmaster's explanation in *Forth Conservancy Board* v. *Inland Revenue Commissioners*[2], and compare what Lord Macmillan said in *Municipal Mutual Insurance Co.* v. *Hills*[3].

Lord Thankerton has conclusively demonstrated that Lord President Inglis' decision in the first *Glasgow Water case* (*Glasgow Water Commissioners* v. *Inland Revenue Commissioners*[4]) falls within this second proposition; so interpreted, it was rightly decided, but it does not help the appellants. The precepts which the appellants issued called for lump sums to be contributed by the two urban district councils which they might pay either from their respective district funds or by levying rates. They were not agents for the appellants in finding the money, but distinct parties. It is true that if either of the councils did not provide the money, the appellants, instead of suing it, might itself by precept empower an officer of their own to raise the necessary amount by levying a rate in place of the defaulting authority, but the substance of the matter is that there is no such identity between contributors and recipients as removes the appellants from the application of the first proposition set out above.

I move that the appeal be dismissed with costs.

(1) (1937) 20 Tax Cas. 643.
(2) (1931) 16 Tax Cas. 103.
(3) (1932) 16 Tax Cas. 430.
(4) (1875) 1 Tax Cas. 28.

LORD THANKERTON.—The subject-matter of this appeal arises upon an assessment made upon the appellant board under Case I of Schedule D of the Income Tax Act, 1918, in the estimated sum of £10,000 for the year 1939-1940 in respect of the profits of its trade, which was that of an undertaking for the supply of water. The only question argued before this House was whether certain sums paid, under precept, to the appellant board by the Pontypridd Urban District Council and the Rhondda Urban District Council under Section 91 of the Pontypridd and Rhondda Water Act, 1910, fall to be included as receipts in the computation of the appellant board's trade profits.

The Commissioners for General Purposes of the Income Tax for the division of Miskin in the county of Glamorgan held that these sums received under precept were not trading receipts and should not be included, and, on the requisition of the Crown, stated a case for the opinion of the High Court of Justice. It may be mentioned that there was also a dispute as to whether a sum paid by the appellant board to the Taf Fechan Water Supply Board should be allowed as a deduction; the General Commissioners held that it should be so allowed, and this conclusion was affirmed in the King's Bench Division and in the Court of Appeal, and the Crown did not press for its disallowance before this House. That point accordingly requires no further mention. On appeal, the decision of the General Commissioners that the sums received under precept by the appellant board were not trading receipts and should not be included in the computation of profits was affirmed by Macnaghten, J., but an appeal by the Crown to the Court of Appeal was allowed, and it was held that the sums in question were trading receipts and should enter into computation. Hence this appeal by the appellant board.

Counsel for the appellant board referred to reasons Nos. 6 and 7 of the appellant's case as embodying his main contentions. These are: (6) where a local authority carries on a commercial undertaking at a loss, and is permitted to make good that loss by a compulsory rate levied on the ratepayers, the amount of the rate so raised is not a receipt of the local authority's said trade, and (7) the board's position in respect of the sum raised by precept to meet its trading losses is similar to that of a local authority, its "ratepayers" being either the two councils, the Rhondda Urban District Council and the Pontypridd Urban District Council as its constituent authorities, or the individual ratepayers of those two districts.

The appellant board was established as a corporate body by a local Act, the Pontypridd and Rhondda Water Act, 1910, the board being constituted as follows: (*a*) The chairman for the time being of the Rhondda Urban District Council; (*b*) the chairman for the time being of the Pontypridd Urban District Council; (*c*) six members to be appointed by the Rhondda

Urban District Council; (*d*) four members to be appointed by the Pontypridd Urban District Council; and it was provided that no one was qualified to be a member of the board unless he was a member of either of these two urban district councils, these two councils being referred to in the Act as "the constituent authorities."

Under Sections 58 and 59 of the Act of 1910, as amended by Section 25 (6) of the Pontypridd and Rhondda Water Act of 1913, the limits of supply within which the board are authorised to supply water direct to consumers are (1) the Pontypridd urban district, and (2) part only of the Rhondda urban district, but in addition the Board was authorised to sell water in bulk to the water undertakers in (1) the Llantrisant and Llantwit Fardre rural district, and (2) part of the Caerphilly urban district. The maximum charges which may be made by the board for supplies taken by consumers within the limits of supply are fixed by Sections 61, 67 and 68 of the Act of 1910; Sections 26 and 27 of the Act of 1913, and Section 18 of the Pontypridd and Rhondda Water Act of 1925. The maximum permitted charges have at all material times been charged by the board.

The payments received by the board from the persons to whom water is supplied consists of (*a*) payments made direct to the board by the consumers within the limits of supply, and (*b*) payments made by the water undertakers in the Llantrisant and Llantwit Fardre rural district and part of the Caerphilly urban district for water sold to them in bulk. It is admitted that both these classes of payments are trade receipts. In addition further sums are received by the board by virtue of Section 91 of the Act of 1910, the material portion of which provides as follows: "91.—(1) Before the first day of April in each year or so soon thereafter as may be practicable the board shall make or cause to be made an estimate of the probable revenue and expenditure other than capital expenditure which will be received and incurred respectively during the year beginning on that day and if such estimate shows that their will be a deficiency in the net revenue of the board for the year the board are hereby authorised and required in every case forthwith to apportion the sum required to meet such deficiency between the constituent authorities in accordance with the provisions of this section. (2) The sum required to meet any deficiency whether for satisfying past or future liabilities shall be apportioned between and borne by the constituent authorities in the proportion which the assessable value of the Pontypridd district bears to the assessable value of that part of the Rhondda district which is within the limits of supply. (3) The board shall issue precepts to the constituent authorities for the amounts apportioned in pursuance of this section and the constituent authorities respectively shall within three months from the receipt of such precepts pay to the

board the amount so apportioned to them respectively. (4) Such amounts respectively shall be paid by the constituent authorities out of their respective district funds and general district rates which funds and rates are hereby charged with the payment of the same accordingly and the constituent authorities respectively are hereby authorised and required to make and levy any rate that may be necessary for the purposes of this section."

Sub-section (5) of Section 91 provides that in default of payment by a constituent authority of the amount so apportioned to it, the board may sue the defaulting authority, or itself cause a rate to be levied in the district of such authority, in order to secure payment. Pursuant to Section 91, the board made an estimate, which showed an estimated deficiency of £ 9,930 in the net revenue of the board for the period ending March 31, 1939, and issued precepts on the constituent authorities for the respective sums apportioned to them out of the said amount. These sums were duly paid by the constituent authorities, and an appropriation account of the board for that year showed the amount of £ 9,930 as received under these precepts. The question at issue is whether the sums thus received under precept to meet an estimated deficiency in the result of what are admittedly trading activities, fall to be taken into account in computing the profits and gains of the board's trade under Case I of Schedule D.

Counsel for the appellant board submitted in the first place that the amounts of the precepts were not to be included among its trade receipts, in view of the decision in the case usually referred to as the *First Glasgow Case* (*Glasgow Water Commissioners* v. *Inland Revenue Commissioners*)[1], with which he maintained the present case was *in pari casu*. In the second place, he contended that the sums in question were not trade receipts (*a*) on general grounds, and (*b*) that they were in exactly the same category as a local rate raised by a public body for the assistance of an undertaking carried on by that body, which is entitled to have such assistance.

The first of these contentions appears to me to involve the question whether the appellant board is entitled to the benefit of the well recognised principle of the exemption of public rating authorities from taxation in respect of the surplus of rates, which is defined by Lord Buckmaster in *Forth Conservancy Board* v. *Inland Revenue Commissioners*[2] as follows: "The principle of exemption for the surplus of rates is, I think, to be found in this, that the rating authority collects money from the inhabitants of the district for the purpose of application to the expenses incurred on behalf of the inhabitants, and that any surplus rightly belongs to the inhabitants themselves, who receive its benefits in case of any surplus, because it is carried forward towards the expenses of the ensuing year."

(1) (1875) 1 Tax Cas. 28. (2) (1931) 16 Tax Cas. 103.

This principle had already been recognised before the *First Glasgow case*[1] in *Attorney-General* v. *Black*[2], in which it was admitted by the Crown that a tax imposed by the community on themselves did not involve liability to income-tax, and, in the Exchequer Chamber, Keating, J., said: " Mr. Manisty does not contend that harbour and port dues, and other revenues of that description, are not taxable; and the Attorney-General admits that a district rate is not. The question then is, does the rate in question partake more of the nature of the one or of the other? I am of opinion that it does not partake of the character of a district rate imposed by the inhabitants of a place upon themselves; and that, on the other hand, it is very difficult to distinguish it from harbour dues." It will be found that this same principle was applied in the *First Glasgow case*[1], which was decided four years later and to which I will now return.

The Glasgow Water Commissioners were created as a statutory incorporation, according to the law of Scotland, by the local Act 18 & 19 Vict. cap. cxviii, by Section 6 of which it was provided: " The magistrates and council of the City of Glasgow and their successors in office for the time being, as representing and for and on behalf of the community of the said city, are hereby appointed commissioners for executing and carrying into effect the purposes of this Act." They were required to furnish the City of Glasgow, that is, within the municipal boundaries, with a supply of water for domestic purposes, and to erect thirty-two public fountains within those boundaries which form the limits of compulsory supply. They were empowered also to deal with parties outside the compulsory limits. Within the limits of compulsory supply the commissioners were entitled to levy two rates, (*a*) a domestic water rate, levied on the occupiers of all dwelling-houses within the area, according to their rents, and (*b*) a public water rate not exceeding a penny in the pound on the full annual value of all premises whatever within the same limits. Both these rates were payable irrespective of whether the ratepayers chose to use the water or not.

After meeting the current expenses of the undertaking, interest on borrowed money and sinking fund charges, the commissioners were required to apply any surplus in reduction of the domestic water rate for the following year. Having been assessed to income tax for the year 1872-1873 in respect of profits to the amount of £17,032 15s., arising upon their undertaking, the water commissioners' appeal was refused by the Commissioners of Property and Income Tax for the City of Glasgow, and a case stated by them came before the First Division of the Court of Session, which allowed the appeal. Lord President Inglis (2 R., at p. 712) said: " Now the sum of £17,032 15s., upon which the charge is made under Schedule D of

(1) (1875) 1 Tax Cas. 28. (2) (1871) 1 Tax Cas. 52.

the Income Tax Act, comprehends the whole portion of the revenue of the water commissioners which is applied towards the formation of the sinking fund in redemption of the annuities and mortgages in the manner that I have already mentioned, and also the balance, if any, which is carried forward to the following year's account, to be applied as the Act directs in reducing the domestic water rate; and the question is, whether income arising from this assessment, which is appropriated to such purposes, is assessable for income tax under Schedule D as profits of this undertaking. I am humbly of opinion that it is not. It seems to me that this is an Act of Parliament by which the citizens of Glasgow have undertaken, through this water corporation as their representatives, to assess themselves for a very important public purpose—a purpose very conducive to their own comfort and well-being—to obtain a good supply of water for the city. In so assessing themselves they had not in view certainly to make profit by the undertaking. On the contrary, what they have distinctly in view is to pay money in order to obtain this particular benefit. They are not, therefore, trading in any commodity, nor are they entering into any undertaking for the use of property that is to be attended by a resulting profit, or a beneficial interest accruing to any individuals, or to any corporation. The object of the assessment is to pay for bringing in the water, and when that is done the assessment and the authority to levy it come to an end." The Lord President then distinguishes the case from the case of *Attorney-General* v. *Black*[1], and *Attorney-General* v. *Scott*[2]. "The case is entirely different from those that have been cited, which have been decided in the Court of Exchequer in England, because in those cases the statute which gave the right to levy the assessment did not impose it upon the citizens of the particular burgh or locality which obtained the Act. It was not an authority to the citizens of a particular locality to assess themselves." The learned Judge then made the reservation which led to the *Second Glasgow case*[3]: "I have only further to say, that if any attempt had been made here to discriminate between that portion of the revenue which arises from the rates levied within the limits of compulsory supply, and that portion of the revenue which is raised in the districts beyond the limits of compulsory supply, I should have been very glad to attend to any grounds which might have been urged for such a distinction." The taxability of profits in respect of the extraneous sources of revenue was raised in *Glasgow Water Commissioners* v. *Miller*[3], in which it was held that, while the rates levied within the compulsory area were to be regarded as sums levied to defray the cost of the water supply within the district, so that any surplus remaining over could not be regarded as profit, any surplus of rates above outlay collected

(1) (1871) 1 Tax Cas. 52.
(2) (1874) 1 Tax Cas. 55.
(3) (1886) 2 Tax Cas. 131.

beyond the compulsory area, or from sales to manufacturers, was profit, which went to reduce the cost of water supply to those within the compulsory area, and was liable to assessment for income tax under Schedule D. Referring to the decision in the earlier case, Lord President Inglis, in delivering the judgment of the Court, said: "We were all of opinion that within the limits of compulsory supply the concern or undertaking as defined by the local Act, was of this nature, that the citizens of Glasgow undertook to assess themselves for accomplishing the important public purpose of supplying the city (being the limits of compulsory supply) with a good supply of pure water; that in doing so they had and could have no view of making profit, for that would have been equivalent to paying out of one pocket and into another pocket of the same individual or class; that they paid these assessments for no other purpose than that of obtaining the particular contemplated benefit, and when that benefit is fully attained and secured for the future the assessment and the authority to levy it come to an end. I have reconsidered that judgment, and have not seen any reason to doubt its soundness."

The significant features of the *Glasgow case* were that (1) the water commissioners were expressly appointed "as representing and for and on behalf of" the community of the City of Glasgow, which formed the area of compulsory supply; (2) the commissioners had the power of levying the domestic and public rates direct on the ratepayers within the compulsory area, and, *quoad* these rates, the ratepayers were ratepayers of the commissioners and not of the municipal corporation; (3) these rates were payable whether the particular ratepayer chose to use the water or not; (4) no price was paid by any domestic consumer for his particular supply and he did not enter into any trading transaction with the commissioners; (5) the rates thus levied were applied to the expenses incurred on behalf of the inhabitants, and any surplus rightly belonged to the ratepayers and was carried forward and applied in reduction of the domestic rate in the next year, thus answering Lord Buckmaster's definition of the principle. On the other hand, the present case is very different. The appellant board (1) are not directly representative of the inhabitants of the Rhondda and Pontypridd Urban District Councils; (2) their limits of supply do not include the whole of the Rhondda urban district; (3) they have no power to levy a rate, except on default of a constituent authority; (4) the sums obtained by precepts under Section 91 are not the expense of obtaining a benefit for the inhabitants of the compulsory area, but are designed to meet a deficiency arising out of the insufficiency of their admitted trading receipts to cover their trading transactions with the individual consumers within the limits of supply, and their sales in bulk—in other words, to make good

their loss in trading; (5) in view of sub-section (4) of Section 91, these sums are not necessarily paid out of the proceeds of any rate, and (6) there is no provision for a public rate, and it would appear that if a constituent authority needed water for any of the purposes usually covered by a public water rate, it would need to enter into a trading transaction with the board. In all these respects the present case is in strong contrast to the *First Glasgow case*[1].

It is true that in the case of the *Forth Conservancy Board* v. *Inland Revenue Commissioners*[2] Lord Buckmaster, while finding it unnecessary for the purposes of that case to examine the soundness of the decision in the *First Glasgow case*, said it appeared difficult to reconcile it with the later decision in this House in *Mersey Docks and Harbour Board* v. *Lucas*[3], and Lord Dunedin expressed a similar doubt. I did not share these doubts, and, as I pointed out, Lord President Inglis had the *Mersey Docks case* before him in the *Second Glasgow case*[4], and reaffirmed his decision in the first case, and the judgment delivered by Lord President Inglis was the judgment of the Court, and in the *Mersey Docks case* two out of the three noble and learned Lords who took part in the decision referred to the *First Glasgow case*. Lord Blackburn approved of the principle on which the Court of Session acted, though not having the Glasgow Act before him, he was not able to say whether a proper construction had been put on it. Lord Fitzgerald clearly found no inconsistency between the decision in the *Glasgow case* and the decision in the *Mersey Docks case*. Having again considered the matter, I am unable to find any inconsistency between the decisions in these two cases.

The appellants' counsel's claim to come within the principle of the *First Glasgow case* not only fails, in my opinion, but in stating the various points of contrast between the provisions of the Glasgow Water Act and the provisions of the appellant board's Water Act, the various matters I have indicated in respect of the latter Act go far to show that the amount of the precepts are not in the position claimed under head (*b*) of his second contention, namely, that they were in exactly the same category as a local rate raised by a public body for the assistance of an undertaking carried on by that body, which is entitled to have such assistance. But I will deal first with head (*a*) of his second contention, by which he contended on general grounds that the sums in question were not trade receipts. In regard to this contention he cited two cases, the first of which was *Seaham Harbour Dock Co.* v. *Crook*[5], which was decided by this House in 1931. The Harbour Dock Co. had applied for and obtained grants from the Unemployment

(1) (1875) 1 Tax Cas. 28.
(2) (1931) 16 Tax Cas. 103.
(3) (1883) 2 Tax Cas. 25.
(4) (1886) 2 Tax Cas. 131.
(5) (1931) 16 Tax Cas. 333.

Grant Committee from funds appropriated by Parliament; these grants were paid as the work progressed and were equivalent to half the interest on approved expenditure met out of loans. The payments were made several times a year for some years. It was held that they were not to be brought into account in computing annual profits or gains. Lord Buckmaster said: "It was a grant by a Government Department with the idea that by its use men might be kept in employment. It was not a trade receipt." Lord Atkin said: "When received, they were received by the appropriate body not as part of their profits or gains or as a sum which went to make up the profits or gains of their trade." I am unable to regard the sums here in question as falling into the same category as the unemployment grants; on the contrary, they were received "as a sum which went to make up the profits or gains of their trade."

The other case cited was *Lincolnshire Sugar Co.* v. *Smart*[1], in which advances made under the British Sugar Industry (Assistance) Act, 1931, to a company carrying on business as manufacturers of sugar beet were held to be trading receipts of the company and liable to income tax under Case I of Schedule D. The language of my noble and learned friend Lord Macmillan in describing the nature of these advances seems to be equally applicable to the sums in question in this appeal. Lord Macmillan, in whose opinion the other four noble and learned Lords concurred, said: "It was with the very object of enabling them to meet their trading obligations that the 'advances' were made; they were intended artificially to supplement their trading receipts so as to enable them to maintain their trading solvency." In my opinion, these two cases afford sufficient reason for rejection of counsel's contention that, on general grounds, the sums here in question are not trading receipts.

In addition to what I have already said as to head (*b*) of counsel's second contention, I will only add that the two cases last cited show that if, as in my opinion, was the case here, the assistance is given for the purpose of being used in the business carried on by the appellant board, so as to enable them to meet their trading obligations, the amounts so given are trading receipts, and this contention also fails.

I have so far expressed my own opinion, but I would like to express my general agreement with the reasons given in the judgments in the Court of Appeal. Accordingly, I am of opinion that the appeal should be dismissed with costs and that the order of the Court of Appeal should be affirmed.

LORD WRIGHT (read by Lord Thankerton).—My Lords, I agree with the speech which has just been delivered by my noble and learned friend Viscount Simon, and do not desire to add anything to it.

(1) (1937) 20 Tax Cas. 643.

LORD THANKERTON.—My Lords, I have been asked by my noble and learned friend LORD PORTER to say that he concurs in the opinion which has been delivered.

LORD SIMONDS.—My Lords, I concur.

Appeal dismissed.

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1946

STATUTES

REPEALING ORDINANCE, 1946.*

(No. I of 1946).

An Ordinance to repeal certain Ordinances.

Whereas an emergency has arisen which makes it necessary to repeal, wholly or partially, certain Ordinances;

Now, therefore, in exercise of the powers conferred by Section 72 of the Government of India Act, as set out in the Ninth Schedule to the Government of India Act, 1935 (26 Geo. 5, c. 2), the Governor-General is pleased to make and promulgate the following Ordinance :—

1. **Short title and commencement.**—(1) This Ordinance may be called the Repealing Ordinance, 1946.

(2) It shall come into force at once.

2. **Repeal of certain Ordinances.**—The Ordinances specified in the Schedule are hereby repealed to the extent mentioned in the fourth column thereof.

3. **Savings.**—The repeal by this Ordinance of any Ordinance shall not affect—

(*i*) the previous operation of any Ordinance so repealed or the validity, invalidity, effect or consequences of anything already done or suffered thereunder, or

(*ii*) any right, title, privilege, obligation or liability acquired, accrued or incurred thereunder, or any release or discharge already granted of or from any debt, penalty, obligation, liability, claim or demand, or any indemnity already granted, or the proof of any past act or thing, or

(*iii*) any penalty, forfeiture or punishment incurred in respect of any offence committed against any Ordinance so repealed, or

(*iv*) any investigation, legal proceeding or remedy in respect of any such right, title, privilege, obligation, liability, penalty, forfeiture or punishment as aforesaid;

and any such investigation, legal proceeding or remedy may be instituted, continued or enforced, and any such penalty, forfeiture or punishment may be imposed, as if this Ordinance had not been made;

nor shall the repeal by this Ordinance of—

(*a*) any Ordinance by which the text of any law was amended by the express omission, insertion or substitution of any matter, affect the continuance of any such amendment in operation at the commencement of this Ordinance, unless a different intention was expressly stated in the Ordinance by which the amendment was made;

* Published in the Gazette of India extraordinary dated January 5, 1946.

(*b*) any Ordinance which was expressed to have any retrospective effect or operation, affect or prejudice in any way such retrospective effect or operation;

nor shall this Ordinance revive or restore anything not in force or existing at the time of its commencement, or affect any law in which any Ordinance hereby repealed has been applied, incorporated or referred to, or affect any principle or rule of law, or established jurisdiction, form or course of pleading, practice or procedure, or existing usage, custom, privilege, restriction, exemption, office or appointment, notwithstanding that they respectively may have been in any manner affirmed, recognised or derived by, in or from any Ordinance hereby repealed.

4. Special provisions in regard to Ordinance XXXVII of 1943.—For the avoidance of doubts it is hereby declared—

(*a*) that notwithstanding the repeal by this Ordinance of the Military Operational Area (Special Powers) Ordinance, 1943, any trial commenced before a Military Court constituted under that Ordinance and not concluded before the commencement of this Ordinance may be proceeded with by that Court, and all the provisions of that Ordinance shall continue to apply to the trial and to any sentence or order passed therein;

(*b*) that any offence committed before the commencement of this Ordinance which would but for the repeal of the said Ordinance have been triable only by a Military Court constituted under that Ordinance may, if the provisions of clause (*a*) are not applicable, be inquired into and tried in accordance with the provisions of the Code of Criminal Procedure, 1898 (V of 1898), by a Court of competent jurisdiction under that Code:

Provided that nothing in clause (*b*) shall be construed as rendering the provisions of Section 22, Section 23 or Section 24 of the said Ordinance applicable to any offence not tried by a Military Court under the said Ordinance.

THE SCHEDULE.

ORDINANCES REPEALED.*

(*See Section 2*).

Year 1	No. 2	Short title 3	Extent of repeal 4
		* * *	
1943	XVI	The Excess Profits Tax Ordinance, 1943.	Sections 3, 4 and 5.
		* * *	
1944	VIII	The Excess Profits Tax (Amendment) Ordinance, 1944.	The whole.
		* * *	
1944	XXXIII	The Indian Finance (Amendment) Ordinance, 1944.	The whole.
		* * *	

* Only the relevant Ordinances are printed here.—Ed.

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STATUTES

THE INDIAN FINANCE ACT, 1946.

(ACT NO. VII OF 1946)

(Received the assent of the Governor-General on the 30th March 1946).

An Act to give effect to the financial proposals of the Central Government for the year beginning on the 1st day of April 1946.

WHEREAS it is expedient to fix the duty on salt manufactured in, or imported by land into, British India, to fix maximum rates of postage under the Indian Post Office Act, 1898 (VI of 1898), to continue, subject to certain modifications, for a further period of one year the additional duties of customs imposed by Section 6 of the Indian Finance Act, 1942 (XII of 1942), to alter the duty of customs on cinematograph films, raw cotton and silver, to withdraw the duty of customs on raw cotton levied under the Cotton Fund Ordinance, 1942 (VIII of 1942), to impose a duty of customs on gold, to alter the duty of customs and the duty of excise on betelnuts, motor spirit, kerosene and mineral oils, to fix rates of income-tax and super-tax, and to make certain provisions relating to income-tax, super-tax and excess profits tax ;

It is hereby enacted as follows :—

1. *Short title and extent.*—(1) This Act may be called the Indian Finance Act, 1946.

(2) It extends to the whole of British India.

2. *Fixation of salt duty.*—The duty on salt manufactured in, or imported by land into, British India shall, for the year beginning on the 1st day of April 1946, be at the rate of one rupee and nine annas per standard maund.

3. *Inland postage rates.*—For the year beginning on the 1st day of April 1946, the Schedule contained in the First Schedule to the Indian Finance Act, 1945, shall again be inserted in the Indian Post Office Act, 1898 (VI of 1898), as the First Schedule to that Act.

4. *Amendment of Section 4, Indian Finance Act, 1945.*—(1) To sub-section (2) of Section 4 of the Indian Finance Act, 1945, the following shall be added, namely :—

" or, after the 28th day of February 1946, on kerosene and mineral oils, comprised in Items Nos. 27 (4) and 27 (5) of the said Schedule."

(2) The provisions of this section shall be deemed to have come into foce on the 28th day of February 1946.

5. *Continuation of, and enhancement of, additional duties of customs imposed by Section 6, Act XII of 1942.*—(1) The additional duties of customs on certain goods chargeable with a duty of customs under the First Schedule to the Indian Tariff Act, 1934 (XXXII of 1934), or under the said Schedule read with any notification of the Central Government for the time being in force, imposed up to the 31st day of March 1943 by Section 6 of the Indian Finance Act, 1942, and continued, subject to certain modifications, up to the 31st day of March 1946, by Section 4 of the Indian Finance Act, 1945, as amended by Section 4 of this Act, shall continue to be levied and

collected as provided in the said Section 6 up to the 31st day of March 1947, subject to the aforesaid modifications and to the further modifications contained in sub-section (2).

(2) The additional duty to be levied and collected under sub-section (1) shall be one-half instead of one-fifth of the amount of the duty of customs specified in the First Schedule to the Indian Tariff Act, 1934, in the case of wines, comprised in Item No. 22 (3) of the said Schedule; and no such additional duty shall be levied or collected on—

(a) betelnuts, comprised in Item No. 9 (5),

(b) cinematograph films, not exposed and exposed, comprised in Items Nos. 29 and 29 (1),

(c) raw cotton, comprised in Item No. 46 (3),

(d) silver bullion and silver sheets and plates which have undergone no process of manufacture subsequent to rolling, and silver coin, not otherwise specified, comprised in Items Nos. 61 (2) and 62 (1),

(e) gold bullion and gold sheets and plates which have undergone no process of manufacture subsequent to rolling, and gold coin, comprised in Items Nos. 61 (3) and 62 (2),

of the said Schedule.

6. *Imposition and alteration of certain duties of customs.*—In the First Schedule to the Indian Tariff Act, 1934 (XXXII of 1934),—

(a) in Item No. 9 (5), for the entries in the fourth and sixth columns, the entries " Five annas per lb." and " Four annas and six pies per lb." shall be respectively substituted;

(b) in Item No. 29, for the entry in the fourth column, the entry " Three pies per linear foot " shall be substituted;

(c) in Item No. 29 (1), for the entry in the fourth column, the entry " Four annas per linear foot " shall be substituted;

(d) in Item No. 46 (3), for the entry in the fourth column, the entry " Two annas per lb." shall be substituted;

(e) in Items Nos. 61 (2) and 62 (1), in the fourth column, for the word " Three " the word " Eight " shall be substituted;

(f) in Items Nos. 61 (3) and 62 (2),—

(i) in the third column the word " Revenue " shall be inserted, and

(ii) for the entry in the fourth column, the following entry shall be substituted, namely:—

" Rs. 25 per tola of 180 grains fine."

7. *Alteration of duty of customs on kerosene and mineral oils.*—In the first Schedule to the Indian Tariff Act, 1934 (XXXII of 1934), in Items Nos. 27 (4) and 27 (5), in the fourth column, the words " and nine pies " shall be omitted.

8. *Alteration of duty of excise on motor spirit.*—(1) In the First Schedule to the Central Excises and Salt Act, 1944 (I of 1944), in item No. 4, for the word " Fifteen " the word " Twelve " shall be substituted.

(2) The provisions of this section shall be deemed to have come into force on the 1st day of March 1946.

9. *Alteration of duty of excise on betelnuts.*—In the First Schedule to the Central Excises and Salt Act, 1944 (I of 1944), in item No. 12, for the words " two annas " the words " one anna " shall be substituted.

10. *Repeal of Ordinance VIII of 1942.*—The Cotton Fund Ordinance, 1942, is hereby repealed:

Provided that the repeal of the said Ordinance shall not prejudice the power of the Central Government to utilise the balance at the credit of the fund established thereunder for the purposes set out in Section 3 of that Ordinance.

11. *Income-tax and super-tax.*—(1) Subject to the provisions of sub-sections (3), (4), (5), (6) and (7),—

(a) income-tax for the year beginning on the 1st day of April 1946 shall be charged at the rates specified in Part I of the Schedule, and

(b) rates of super-tax for the year beginning on the 1st day of April 1946 shall, for the purposes of Section 55 of the Indian Income-tax Act, 1922 (XI of 1922), be those specified in Part II of the Schedule.

(2) In making any assessment for the year ending on the 31st day of March 1947, there shall be deducted from the total income of an assessee, in accordance with the provisions of Section 15A of the Indian Income-tax Act, 1922, an amount equal to—

(i) one-tenth of the earned income chargeable under the head "Salaries" which is included in his total income, subject to a maximum of two thousand rupees, *plus*

(ii) one-fifth of the earned income other than the income chargeable under the head "Salaries" which is included in his total income:

Provided that the aggregate amount to be deducted under this sub-section shall not in any case exceed four thousand rupees.

(3) In making any assessment for the year ending on the 31st day of March 1947,—

(a) where the total income of an assessee, not being a company, includes any income chargeable under the head "salaries" as reduced by the deduction for earned income appropriate thereto, or any income chargeable under the head "Interest on Securities," or any income from dividends in respect of which he is deemed under Section 49B of the Indian Income-tax Act, 1922, to have paid income-tax imposed in British India, the income-tax payable by the assessee on that part of his total income which consists of such inclusions shall be an amount bearing to the total amount of income-tax payable according to the rates applicable under the operation of the Indian Finance Act, 1945, on his total income the same proportion as the amount of such inclusions bears to his total income;

(b) where the total income of an assessee, not being a company, includes any income chargeable under the head "Salaries" on which super-tax has been or might have been deducted under the provisions of sub-section (2) of Section 18 of the Indian Income-tax Act, 1922, the super-tax payable by the assessee on that portion of his total income which consists of such inclusion shall be an amount bearing to the total amount of super-tax payable according to the rates applicable under the operation of the Indian Finance Act, 1945, on his total income the same proportion as the amount of such inclusion bears to his total income.

(4) In making any assessment for the year ending on the 31st day of March 1947, where the total income of an assessee consists partly of earned income and partly of unearned income, the super-tax payable by him shall be—

(i) on that part of the earned income chargeable under the head "Salaries" to which clause (b) of sub-section (3) applies, the amount of super-tax computed in accordance with the provisions of that clause, *plus*

(ii) on the remainder of the earned income, the amount which bears to the total amount of super-tax which would have been payable on his total income had it consisted wholly of earned income the same proportion as such remainder bears to his total income, *plus*

(iii) on the unearned income, the amount which bears to the total amount of super-tax which would have been payable on his total income had it consisted wholly of unearned income the same proportion as the unearned income bears to his total income.

(5) Where the total income of an assessee referred to in paragraph A of Part I of the Schedule does not exceed six thousand rupees and includes any income to which clause (a) of sub-section (3) applies, the income-tax payable by the assessee on such inclusion as computed in accordance with the provisions of that clause shall be reduced by an amount representing one rupee for every complete unit of two hundred rupees of such inclusion as reduced by the amount of income, if any, exempt under the second proviso to sub-section (1) of Section 7, Section 15, and sub-section (1) of Section 58F, of the Indian Income-tax Act, 1922 :

Provided that the reduction to be made under this sub-section shall not in any case exceed two-fifths of the income-tax otherwise payable on such inclusion :

Provided further that if there is an incomplete unit of such inclusion amounting to one hundred rupees or more, it shall for the purposes of this sub-section be reckoned as a complete unit of two hundred rupees.

(6) In making any assessment for the year ending on the 31st day of March 1947,—

(a) Where the total income of a company includes any profits and gains from life insurance business, the super-tax payable by the company shall be reduced by an amount computed at the rate of one anna in the rupee on that part of its total income which consists of such inclusion;

(b) where the total income of an assessee, not being a company, includes any profits and gains from life insurance business, the income-tax and super-tax payable by the assessee on that part of his total income which consists of such inclusion shall be an amount bearing to the total amount of such taxes payable according to the rates applicable under the operation of the Indian Finance Act, 1942 (XII of 1942), on his total income the same proportion as the amount of such inclusion bears to his total income, so however, that the aggregate of the taxes so computed in respect of such inclusion shall not in any case exceed the amount of tax payable on such inclusion at the rate of five annas in the rupee.

(7) In cases to which Section 17 of the Indian Income-tax Act, 1922, applies, the tax chargeable shall be determined as provided in that section but with reference to the rates imposed by sub-section (1) of this section and in accordance, where applicable, with the provisions of sub-sections (3), (4), (5) and (6) of this section.

(8) For the purposes of making any deduction of income-tax in the year beginning on the 1st day of April 1946, under sub-section (2) or sub-section (2B) of Section 18 of the Indian Income-tax Act, 1922, from any earned income chargeable under the head " Salaries," the estimated total income of the assessee under this head shall, in

computing the income-tax to be deducted, be reduced by an amount equal to one-fifth of such earned income but not exceeding in any case four thousand rupees.

(9) For the purposes of this section and of the rates of tax imposed thereby, the expression "total income" means total income as determined for the purposes of income-tax or super-tax, as the case may be, in accordance with the provisions of the Indian Income-tax Act, 1922, and the expression "earned income" has the meaning assigned to it in clause (6AA) of Section 2 of that Act.

(10) If any provision is made in the Indian Income-tax Act, 1922, for the allowance of expenditure on scientific research related to the business carried on by an assessee, then any such expenditure incurred by him in the previous year for the assessment for the year ending on the 31st day of March 1946 shall, for the purposes of that provision and in accordance therewith, be deemed to be expenditure incurred in the previous year for the assessment for the year ending on the 31st day of March 1947, and shall be added to the amount of such expenditure, if any, in that previous year.

(11) Any sum being excess profits tax repaid in respect of any chargeable accounting period under the provisions of Section 10 of the Indian Finance Act, 1942, or of Section 2 of the Excess Profits Tax Ordinance, 1943 (XVI of 1943), shall be deemed to be income for the purposes of the Indian Income-tax Act, 1922, and shall, notwithstanding the provisions of Section 34 of that Act, be treated as income of the previous year which constitutes or includes the chargeable accounting period in respect of which the said sum is repayable :

Provided that any such sum repaid in respect of any profits which are also assessable to excess profits tax under the law in force in the United Kingdom shall be treated, for the purpose of assessment to income-tax and super-tax, as income of the previous year during which the repayment is made.

(12) The Income-tax Officer shall calculate the amount of income-tax and super-tax payable in respect of each sum referred to in sub-section (11), and such amount shall be deducted from the said sum at the time that it is repaid, and where the regular assessment proceedings for the appropriate assessment year are not complete, the tax so deducted shall be treated as a payment of income-tax or super-tax, as the case may be, for the purposes of sub-section (5) of Section 18 of the Indian Income-tax Act, 1922.

(13) Any person objecting to the amount of a deduction made under sub-section (12) may appeal to the Appellate Assistant Commissioner within thirty days of the receipt of the repayment order, and the provisions of Sections 30, 31 and 33 of the Indian Income-tax Act, 1922, shall apply as if such appeal were an appeal under the first mentioned section.

(14) Where under the provisions of sub-section (2) of Section 12 of the Excess Profits Tax Act, 1940 (XV of 1940), excess profits tax payable under the law in force in the United Kingdom has been deducted in computing for the purposes of income-tax and super-tax the profits and gains of any business, the amount of any repayment under sub-section (1) of Section 28 of the Finance Act, 1941 (4 & 5 Geo. 6, c. 30), as amended by Section 37 of the Finance Act, 1942 (5 & 6 Geo. 6, c. 21), in respect of those profits, shall be deemed to be income for the purposes of the Indian Income-tax Act, 1922, and shall, for the

purpose of assessment to income-tax and super-tax, be treated as income of the previous year during which the repayment is made.

12. *Excess profits tax.*—If any provision is made in clause (vi) of sub-section (2) of Section 10 of the Indian Income-tax Act, 1922 (XI of 1922), to allow in respect of depreciation a further sum which is not deductible in determining the written down value, then such sum shall not be included in the allowances made in computing profits for the purposes of the Excess Profits Tax Act, 1940 (XV of 1940).

13. *Amendment of Section 10, Act XII of 1942.*—(1) To sub-section (1) of Section 10 of the Indian Finance Act, 1942, the following further proviso shall be added, namely :—

"Provided further that no such further sum herein referred to shall be deposited with the Central Government after the 28th day of February 1946."

(2) The provisions of this section shall be deemed to have come into force on the 28th day of February 1946.

THE SCHEDULE.

(See Section 11).

PART I. Rates of Income-tax.

A.—In the case of every individual, Hindu undivided family, unregistered firm and other association of persons not being a case to which paragraph B of this Part applies— Rate.

1. On the first Rs. 1,500 of total income—Nil.
2. On the next Rs. 3,500 of total income—One anna in the rupee.
3. On the next Rs. 5,000 of total income—Two annas in the rupee.
4. On the next Rs. 5,000 of total income—Three and a half annas in the rupee.
5. On the balance of total income—Five annas in the rupee.

Provided that—

(i) no income-tax shall be payable on a total income which, before deduction of the allowance, if any, for earned income, does not exceed Rs. 2,000 ;

(ii) the income-tax payable shall in no case exceed half the amount by which the total income (before deduction of the said allowance, if any, for earned income) exceeds Rs. 2,000 ;

(iii) the income-tax payable on the total income as reduced by the allowance for earned income shall not exceed either—

(a) a sum bearing to half the amount by which the total income (before deduction of the allowance for earned income) exceeds Rs. 2,000 the same proportion as such reduced total income bears to the unreduced total income, or

(b) the income-tax payable on the income so reduced at the rates specified in this Schedule,

whichever is less.

B.—In the case of every company and local authority, and in every case in which under the provisions of the Indian Income-tax Act, 1922, income-tax is to be charged at the maximum rate—

Rate.

On the whole of total income . . . . Five annas in the rupee.

PART II. Rates of Super-tax.

A.—In the case of every individual, Hindu undivided family, unregistered firm and other association of persons, not being a case to

which paragraph B or paragraph C or paragraph D of this Part applies—

	Rate, if income wholly earned.	Rate, if income wholly unearned.
1. On the first Rs. 25,000 of total income ...	Nil.	Nil.
2. On the next Rs. 10,000 of total income ...	Two annas in the rupee.	Three annas in the rupee.
3. On the next Rs. 10,000 of total income ...	Three annas in the rupee.	Four annas in the rupee.
4. On the next Rs. 15,000 of tolal income ...	Four annas in the rupee.	Five annas in the rupee.
5. On the next Rs. 20,000 of total income ...	Five annas in the rupee.	Six annas in the rupee.
6. On the next Rs. 30,000 of total income ...	Six annas in the rupee.	Seven annas in the rupee.
7. On the next Rs. 40,000 of total income ...	Seven annas in the rupee.	Eight annas in the rupee.
8. On the next Rs. 50,000 of total income ...	Eight annas in the rupee.	Nine annas in the rupee.
9. On the next Rs. 50,000 of total income ...	Nine annas in the rupee.	Nine and a half annas in the rupee.
10. On the next Rs. 1,00,000 of total income...	Nine and a half annas in the rupee.	Ten annas in the rupee.
11. On the next Rs. 1,50,000 of total income...	Ten annas in the rupee.	Ten and a half annas in the rupee
12. On the balance of total income ...	Ten and a half annas in the rupee.	Ten and a half annas in the rupee

B.—In the case of every local authority—

Rate.

On the whole of total income...........One anna in the rupee.

C.—In the case of an association of persons being a co-operative society, other than the Sanikatta Saltowners' Society in the Bombay Presidency, for the time being registered under the Co-operative Societies Act, 1912, or under an Act of the Provincial Legislature governing the registration of co-operative societies—

Rate.

1. On the first Rs. 25,000 of total income.........Nil.
2. On the balance of total income.........One anna in the rupee.

D.—In the case of every company—

Rate.

On the whole of total income.................One anna in the rupee.
and in addition, in respect of that part of the total income (as reduced by the amount of dividends payable at a fixed rate) which does not exceed the amount of dividends, not being dividends payable at a fixed rate, declared in British India in respect of the whole or part of the previous year for the assessment for the year ending on the 31st day of March 1947,—
on the amount by which such part—

	Rate.
(*a*) exceeds 30 per cent., but does not exceed 40 per cent., of the total income as so reduced.	Two annas in the rupee.
(*b*) exceeds 40 per cent., but does not exceed 45 per cent., of the total income as so reduced.	Three annas in the rupee.
(*c*) exceeds 45 per cent., but does not exceed 50 per cent., of the total income as so reduced.	Four annas in the rupee.
(*d*) exceeds 50 per cent., but does not exceed 55 per cent., of the total income as so reduced.	Five annas in the rupee

	Rate.
(e) exceeds 55 per cent., but does not exceed 60 per cent., of the total income as so reduced.	Six annas in the rupee.
(f) exceeds 60 per cent., of the total income as so reduced.	Seven annas in the rupee.

Provided that—

(i) no additional super-tax shall be payable where such part is less than, or equal to, five per cent. on the capital of the company;

(ii) where such part is more than five per cent. on the capital of the company, the additional super-tax payable shall be reduced by the amount of additional super-tax which would, but for the provisions of clause (i) of this proviso, have been payable had such part been equal to five per cent. on the capital of the company;

(iii) where any dividends (not being dividends payable at a fixed rate) have been declared before the 1st day of March 1946 in respect of the whole or part of the previous year for the assessment for the year ending on the 31st day of March 1947, and the amount of super-tax computed at the rates set out in this paragraph exceeds the amount of super-tax which would be payable by the company at the rate specified in the Indian Finance Act, 1945, such proportion of the amount of super-tax computed under this paragraph as the amount of dividends declared before the 1st day of March 1946 bears to the total amount of dividends declared in respect of the said previous year (not being dividends payable at a fixed rate) shall be so reduced as not to exceed the same proportion of the super-tax computed at the rate specified in the Indian Finance Act, 1945;

(iv) the additional super-tax shall be payable only by a company in which the public are substantially interested within the meaning of the *Explanation* to sub-section (1) of Section 23A of the Indian Income-tax Act, 1922, or a subsidiary company of such a company where the whole of the share capital of such subsidiary company is held by the parent company or by the nominees thereof.

Explanation.—For the purposes of this paragraph,—

(a) the expression "capital of the company" shall be deemed to mean the paid-up share capital at the beginning of the previous year for the assessment for the year ending on the 31st day of March 1947 (other than capital entitled to a dividend at a fixed rate) plus any reserves other than depreciation reserves and reserves for bad or doubtful debts at the same date as diminished by the amount on deposit on the same date with the Central Government under Section 10 of the Indian Finance Act, 1942, or Section 2 of the Excess Profits Tax Ordinance, 1943;

(*b*) the expression "dividend" shall be deemed to include any distribution included in the expression "dividend" as defined in clause (6A) of Section 2 of the Indian Income-tax Act, 1922, and any such distribution made during the year ending on the 31st day of March 1947 shall be deemed to have been made in respect of the whole or part of the previous year;

(*c*) where any portion of the profits and gains of a company is not included in its total income, by reason of such portion being exempt from tax under any provision of the Indian Income-tax Act, 1922, the capital of the company, the total amount of dividends and the amount of dividends payable at a fixed rate shall each be deemed to be the proportion thereof that the total income of the company bears to its total profits and gains.

Income Tax Reports.

VOLUME XIV—1946

STATUTES

INDIAN INCOME TAX (AMENDMENT) ACT, 1946.

(ACT No. VIII OF 1946).

(Received the assent of the Governor-General on the 18th April 1946).

An Act further to amend the Indian Income-tax Act, 1922.

WHEREAS it is expedient further to amend the Indian Income-tax Act, 1922 (XI of 1922), for the purposes hereinafter appearing;

It is hereby enacted as follows :—

1. *Short title and commencement.*—(1) This Act may be called the Indian Income-tax (Amendment) Act, 1946.

(2) It shall come into force on such date as the Central Government may by notification in the official Gazette appoint.

2. *Amendment of Section 4, Act XI of 1922.*—In sub-section (3) of Section 4 of the Indian Income-tax Act, 1922 (hereinafter referred to as the said Act), after clause (xi) the following clause shall be inserted, namely :—

"(xii) Any income chargeable under the head "Income from property" in respect of a building the erection of which is begun and completed between the 1st day of April 1946 and the 31st day of March 1948 (both dates inclusive), for a period of two years from the date of such completion."

3. *Amendment of Section 10, Act XI of 1922.*—In Section 10 of the said Act,—

(a) in sub-section (2),—

(i) in clause (vi), after the words "cases be prescribed" where they occur for the second time, the following shall be inserted, namely :—

"and where the buildings have been newly erected, or the machinery or plant being new has been installed, after the 31st day of March 1945, a further sum (which shall however not be deductible in determining the written down value for the purposes of this clause) in respect of the year of erection or installation equivalent,—

(a) in the case of buildings the erection of which is begun and completed between the 1st day of April 1946 and the 31st day of March 1948 (both dates inclusive), to fifteen per cent. of the cost thereof to the assessee;

(b) in the case of other buildings, to ten per cent. of the cost thereof to the assessee;

(c) in the case of machinery or plant, to twenty per cent. of the cost thereof to the assessee :"

(ii) for clause (vii) the following clause shall be substituted, namely :—

"(vii) in respect of any such building, machinery or plant which has been sold or discarded or demolished or destroyed, the amount by which the written down value thereof exceeds the amount for which the building, machinery or plant, as the case may be, is actually sold or its scrap value :

Provided that such amount is actually written off in the books of the assessee :

Provided further that where the amount for which any such building, machinery or plant is sold exceeds the written down value, so much of the excess as does not exceed the difference between the original cost and the written down value shall be deemed to be profits of the previous year in which the sale took place:

Provided further that where any insurance, salvage or compensation moneys are received in respect of any such building, machinery or plant which has been discarded or demolished or destroyed, and the amount of such moneys does not exceed the written down value, the amount allowable under this clause shall be the amount, if any, by which the difference between the written down value and the scrap value exceeds the amount of such moneys:

Provided further that where any insurance, salvage or compensation moneys are received in respect of any such building, machinery or plant as aforesaid, and the amount of such moneys exceeds the difference between the written down value and the scrap value no amount shall be allowable under this clause and so much of the excess as does not exceed the difference between the original cost and the written down value less the scrap value shall be deemed to be profits of the previous year in which such moneys were received:

Provided further that for the purposes of this clause, the original cost of a building, the written down value of which is determined in accordance with the first proviso to sub-section (5), shall be deemed to be the written down value so determined as at the date of its being brought into use for the purposes of the business, profession or vocation;"

(iii) clause (xii) shall be renumbered as clause (xv), and after clause (xi) the following clauses shall be inserted, namely:—

"(xii) any expenditure (not being in the nature of capital expenditure) laid out or expended on scientific research related to the business;

(xiii) any sum paid to a scientific research association having as its objects the undertaking of scientific research related to the class of business carried on, and any sum paid to a university, college or other institution to be used for such scientific research:

Provided that such association, university, college or institution is for the time being approved for the purposes of this clause by the prescribed authority;

(xiv) in respect of any expenditure of a capital nature on scientific research related to the business, an allowance for each of the five consecutive previous years beginning with the year in which the expenditure was incurred, or where the expenditure was incurred prior to the commencement of the business, for each of the five consecutive previous years beginning with the year in which the business was commenced, equal to one-fifth of such expenditure:

Provided that no allowance shall be made for any expenditure incurred more than three years before the commencement of the business:

Provided further that—

(a) where an asset representing scientific research expenditure of a capital nature ceases to be used for scientific research related to such business—

(i) no allowance shall be made in respect of any previous year after the previous year in which the cessation takes place, and

(ii) if the aggregate of the amounts allowed under this clause added to the value of the asset immediately before the cessation is less than the said expenditure, there shall also be allowed in respect of the previous year in which the cessation takes place an additional deduction equal to the difference;

(b) where such asset is sold without having been used for other purposes, the sale proceeds shall be taken to be the value of the asset immediately before the cessation, and if an additional allowance or a greater additional allowance would have been made in respect of the previous year in which the cessation occurred on the basis of that value, an amount equal to the additional allowance which would have been made or, as the case may be, to the difference between the additional allowance which would have been made and the additional allowance which was made for that year shall be made in respect of the previous year in which the sale occurs;

(c) where the proceeds of the sale plus the total amount of the allowances made under this clause exceed the amount of the expenditure, the excess or the amount of the allowances so made, whichever is the less, shall be treated as a receipt of the business accruing at the time of the sale;

(d) where a deduction is allowed for any previous year under this clause in respect of expenditure represented wholly or partly by any asset, no deduction shall be allowed under clause (vi) or clause (vii) for the same previous year in respect of that asset;

(e) where an asset is used in the business after it ceases to be used for scientific research related to that business, and a claim for an allowance under clause (vi) or clause (vii) is made in respect of that asset, the actual cost to the assessee of the asset shall be treated as reduced by the amount of any deductions allowed under this clause;

(f) clause (b) of the proviso to clause (vi) shall apply in relation to deductions allowable under this clause as it applies in relation to deductions allowable in respect of depreciation;

(g) if any question arises under clause (xii), clause (xiii) or this clause as to whether, and if so to what extent, any activity constitutes or constituted or any asset is or was being used for, scientific research, the Central Board of Revenue shall refer the question to the prescribed authority, whose decision shall be final;

Explanation.—In clause (xii), clause (xiii) and this clause—

(i) "scientific research" means any activities in the fields of natural or applied science for the extension of knowledge;

(ii) references to expenditure incurred on scientific research do not include any expenditure incurred in the acquisition of rights in, or arising out of, scientific research, but, save as aforesaid, include all expenditure incurred for the prosecution of, or the provision of facilities for the prosecution of, scientific research;

(iii) references to scientific research related to a business or class of business include—

(a) any scientific research which may lead to or facilitate an extension of that business or, as the case may be, all businesses of that class;

(b) any scientific research of a medical nature which has a special relation to the welfare of workers employed in that business or, as the case may be, businesses of that class;"

(b) in sub-section (5), after the word "Provided" in the proviso the word "further" shall be inserted, and before the said proviso the following proviso shall be inserted, namely:—

"Provided that in the case of a building previously the property of the assessee and brought into use for the purposes of the business, profession or vocation after the 28th day of February 1946, 'written down value' means the actual cost to the assessee reduced by an amount equal to the depreciation calculated at the rate in force on that date that would have been allowable had the building been used for the aforesaid purposes since the date of its acquisition by the assessee and had the provisions of this Act relating to the allowance for depreciation been in force on and from the date of acquisition."

4. *Amendment of Section 12, Act XI of 1922.*—In sub-section (4) of Section 12 of the said Act, for the brackets, figures and word "(v) and (vi)" the brackets, figures and word "(v), (vi) and (vii)" shall be substituted.

5. *Amendment of Section 41, Act XI of 1922.*—In sub-section (1) of Section 41 of the said Act, to the first proviso the following shall be added, namely:—

"but, where such persons have no other personal income chargeable under this Act and none of them is an artificial juridical person, as if such income, profits or gains or such part thereof were the total income of an association of persons."

STATEMENT OF OBJECTS AND REASONS.

The object of this Bill is to give concessions to the taxpayer mainly for the purpose of encouraging the modernisation and rehabilitation of industry and trade. The proposals include provisions for special initial depreciation allowances in respect of new buildings, plant and machinery, for the allowance of expenditure (both capital and revenue) on scientific research, for obsolescence allowances in respect of buildings used for the purpose of a business, profession or vocation and for obsolescence allowances in respect of machinery or plant that has been demolished or destroyed. In order to encourage the erection of new buildings in the next two years the proposals also include provisions for a two years' exemption in respect of such buildings the income of which is assessable under the head "property" and an additional initial depreciation allowance of 5 per cent. in respect of such buildings is used for the purpose of a business, profession or vocation. The clauses are explained in the notes below.

NOTES ON CLAUSES.

Clause 2.—If a building the income from which is assessable under the head "property" is begun and completed between the 1st April, 1946, and the 31st March, 1948, the income therefrom would be exempt under this clause for two years from the date of completion. The clause mainly applies to buildings which are not used by the owner for the purposes of his business.

Clause 3 (a) (i) proposes special initial depreciation allowances for new buildings, plant and machinery. In the case of buildings the rate will be 10 per cent. of the cost and in the case of plant and machinery

20 per cent. But for buildings begun and completed between the 1st April, 1946, and the 31st March, 1948, the rate will be 15 per cent. The allowance is not to be deducted in computing the written-down value and it is not to be given for excess profits tax purposes (see Finance Bill).

Clause 3 (a) (ii) amends Section 10 (2) (vii). At present what is known as "obsolescence allowance" is given only if plant or machinery is sold or discarded and it is not given in the case of buildings. The amendment proposes to extend the allowance to buildings and to enlarge it so as to include the demolition or destruction of the buildings, plant or machinery. But if any insurance, salvage or compensation moneys are received in respect of these assets, these moneys, if they are less than the written-down value minus the scrap value, will be deducted from the allowance admissible and, if they are greater, the excess will be taxed to the extent of the difference between the original cost and the written-down value less the scrap value. As clause (vii) stands at present, if machinery or plant is sold for more than its original cost, the excess over the original cost is taxable. As now proposed to be amended, the excess over the original cost will not be taxable.

Clause 3 (a) (iii).—This clause proposes to allow expenditure on scientific research related to a business or to the class of business carried on. The first two items, *viz.*, revenue expenditure by the assessee on such scientific research and sums paid to research associations or institutions, will be allowed in the assessments of the profits of the year in which the expenses were incurred. The other item, *viz.*, capital expenditure, will be allowed in five consecutive equal instalments and will be given also in respect of such expenditure incurred not more than three years before the commencement of the business. Provision is also made for allowing the difference between the residual value of an asset representing such expenditure and the amount allowed in the yearly instalments. Other provisions in connection with the allowance safeguard the revenue position, *e.g.*, prevent double allowances or excessive allowances. A provision in the Finance Bill is designed to give retrospective effect for one year to the grant of this allowance.

Clause 3 (b) is designed to safeguard the revenue against an assessee who might seek to take unfair advantage of the provisions regarding depreciation and obsolescence. As the law stands and as it is proposed to be amended in this Bill, apart from this sub-clause, an assessee might, for example, occupy a building as a residence for many years and when the time to scrap it was drawing near bring it into use for the purpose of his business. Without this amendment he would, if he scrapped or demolished the building a year later, get an allowance of the whole of the difference between the original cost and one year's depreciation allowance. It is proposed therefore that in cases like this the written-down value will be the cost less the depreciation that would have been allowable at existing rates and on the written-down value basis if the building had been used for the purposes of the business from the date of its acquisition. It is not proposed to give retrospective effect to the provision.

Clause 4 is consequential on clause 3 (a) (ii).

Clause 5.—Under the proviso in question tax is leviable at the maximum rate where the income is not specifically receivable on

behalf of any one person or where the individual shares are indeterminate and unknown. This causes hardship in some cases, for example in cases of trusts for the maintenance of widows and children where the total income is small. The amendment proposes therefore that tax should be levied in such cases at the rate applicable to the trust income.

REPORT OF THE SELECT COMMITTEE.

The following Report of the Select Committee on the Bill further to amend the Indian Income-tax Act, 1922 (XI of 1922), was presented to the Legislative Assembly on the 25th March, 1946:—

We, the undersigned, members of the Select Committee to which the Bill further to amend the Indian Income-tax Act, 1922 (XI of 1922), was referred, have considered the Bill and have now the honour to submit this our Report with the Bill as amended by us annexed thereto.

We find that it is only in relation to clause 3 of the Bill that we have any comments to make or changes to propose. In this clause we correct a printing error of a single letter at the end of the clause, and propose two insertions in sub-clause (a) (ii), which replaces by a new clause, clause (vii) of Section 10 (2) of the Act.

In the fourth proviso to this new clause (vii), the last proviso included in the Bill as introduced, we propose a small insertion to make it clear that where there is any excess chargeable under that proviso, no allowance shall be given under the substantive provision of the clause on the ground that the written down value of the asset exceeded its scrap value.

We propose the addition of a further proviso to this new clause (vii) to provide that the original cost for the purpose of charging any excess under this clause shall be the written down value as calculated under the new proviso to sub-section (5) of Section 10 of the Act, which is inserted by the concluding provision of clause 3 of the Bill.

In connection with the proposed clauses (xii) to (xiv) of Section 10 (2), sub-clause (a) (iii) of clause 3 of the Bill, we gave consideration to the question whether the proposed definition of "scientific research" was adequate, for instance, whether research into the economic aspects of the business, particularly statistical research was covered. We note however that the definition is taken substantially unchanged from the Act of Parliament on the subject, and in proposing no modification of this definition, we hope that the expression will not be interpreted too narrowly by the authorities concerned.

2. The Bill was published in the *Gazette of India*, dated the 9th March 1946.

3. We think that the Bill has not been so altered as to require republication, and we recommend that it be passed as now amended.

Asoka K. Roy.	Yusuf A. Haroon.
A. Rowlands.	K. C. Neogy.
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Income Tax Reports.

VOLUME XIV—1946.

STATUTES.

APPELLATE TRIBUNAL RULES, 1946*.

In pursuance of sub-section (8) of Section 5-A of the Indian Income-tax Act, 1922 (XI of 1922), and in supersession of the existing rules made thereunder, the Appellate Tribunal is pleased to make the following rules, namely :—

1. (1) These rules may be called the Appellate Tribunal Rules, 1946.

(2) They shall come into force on the 25th November 1946.

2. In these rules, unless there is anything repugnant in the subject or context,—

(*i*) "Act" means the Indian Income-tax Act, 1922 (XI of 1922);

(*ii*) "authorised representative" means—

(*a*) in relation to an assessee, a person duly authorised by the assessee under Section 61 to attend before the Tribunal; and

(*b*) in relation to an income-tax authority who is a party to any proceeding before the Tribunal, a person duly appointed by the Central Government by notification in the Official Gazette as authorised representative to appear, plead and act for such authority in any such proceeding, and any other person acting on behalf of the person so appointed;

(*iii*) "Bench" means a Bench of the Tribunal constituted under sub-section (5) of Section 5-A ;

(*iv*) "member" means a member of the Tribunal;

(*v*) "prescribed form" means a form prescribed in the rules made by the Central Board of Revenue under Section 59 ;

(*vi*) "President" means the President of the Tribunal ;

(*vii*) "Registrar" means the person who is for the time being discharging the functions of the Registrar of the Tribunal ;

(*viii*) "Section" means a section of the Act.

(*ix*) "Tribunal" means the Appellate Tribunal constituted by the Central Government under Section 5-A, and includes where the context so requires, a Bench exercising and discharging the powers and functions of the Tribunal.

3. A Bench shall hold its sittings at its headquarters or such other place as it may consider convenient.

4. A Bench shall hear and determine such appeals and applications made under the Act as the President may by general or special order direct.

* Published in Part II, Section 2 (page 606) of the Gazette of India dated the 16th November, 1946.

5. (1) The office of the Tribunal at Bombay shall, subject to any special order of the President, observe the same office hours and holidays as the office of the High Court at Bombay.

(2) The office of a Bench elsewhere than at Bombay shall, subject to any special order of the Bench, observe the same office hours and holidays as the office of the High Court at the headquarters of the Bench.

6. The language of the Tribunal shall be English.

7. (1) A memorandum of appeal to the Tribunal shall be presented by the appellant in person or by an agent to the Registrar at the headquarters of the Tribunal at Bombay, or to an officer authorised in this behalf by the Registrar, or sent by registered post addressed to the Registrar or to such officer.

(2) A memorandum of appeal sent by post under sub-rule (1) shall be deemed to have been presented to the Registrar or to the officer authorised by the Registrar, on the day on which it is received in the office of the Tribunal at Bombay or, as the case may be, in the office of such officer.

8. The Registrar or, as the case may be, the authorised officer shall endorse on every memorandum of appeal the date on which it is presented, or deemed to have been presented under rule 7 and shall sign the endorsement.

9. Every memorandum of appeal shall be written in English, and shall set forth, concisely and under distinct heads, the grounds of appeal without any argument or narrative; and such grounds shall be numbered consecutively.

10. (1) Every memorandum of appeal shall be in triplicate and shall be accompanied by two copies (at least one of which shall be a certified copy) of the order appealed against and two copies of the order of the Income-tax Officer.

(2) The Tribunal may in its discretion accept a memorandum of appeal which is not accompanied by all or any of the documents referred to in sub-rule (1).

11. Where a fact which cannot be borne out by, or is contrary to, the record is alleged, it shall be stated clearly and concisely and supported by a duly sworn affidavit.

12. The appellant shall not, except by leave of the Tribunal, urge or be heard in support of any ground not set forth in the memorandum of appeal; but the Tribunal, in deciding the appeal, shall not be confined to the grounds set forth in the memorandum of appeal or taken by leave of the Tribunal under this rule.

Provided that the Tribunal shall not rest its decision on any other ground unless the party who may be affected thereby has had a sufficient opportunity of being heard on that ground.

13. The Tribunal may reject a memorandum of appeal, if it is not in the prescribed form or return it for being amended within such time as it may allow. On re-presentation after such amendment the memorandum shall be signed and dated by an officer authorised in this behalf by the Tribunal.

14. In an appeal by an assessee under sub-section (1) of Section 33, the Income-tax Officer concerned shall be made a respondent to the appeal.

15. In an appeal by an Income-tax Officer under sub-section (2) of Section 33, the appellant before the Appellate Assistant Commissioner shall be made a respondent to the appeal.

16. In an appeal under sub-section (2) of Section 33 the Income-tax Officer shall append to the memorandum of appeal a certificate that the appeal has been preferred under the direction of the Commissioner.

17. Where a memorandum of appeal is signed by an authorised representative, such representative shall annex to the memorandum of appeal the writing constituting his authority and his acceptance of it. The acceptance shall be signed and dated by the representative and shall state whether he is a lawyer, an accountant or an Income-tax practitioner, or is a person who is a relative of, or regularly employed by, the assessee. If the representative is a person regularly employed by the assessee, he shall state the capacity in which he is at the time employed; if he is a relative of the assessee, he shall state his relationship with the assessee; and if he is an income-tax practitioner, he shall state his qualifications under clause (iv) of sub-section (2) of Section 61. Provided that in the case of an appeal under sub-section (2) of Section 33, the memorandum of appeal need not be accompanied by a letter of authority.

18. An authorised representative appearing for an assessee at the hearing of an appeal shall, unless he has already filed his authority and his acceptance of it under rule 17, before the commencement of the hearing file his authority and his acceptance of authority containing the particulars required by rule 17.

19. The Tribunal may, on an application made by an appellant, direct the preparation of a paper book at the cost of the appellant. If such a direction is given, the parties to the appeal shall be required by the Registrar to state what papers and documents they desire to be included in the paper book. On receipt of the statements of the parties, the Registrar shall take such action as may be necessary for the preparation of the paper book.

20. The Tribunal shall notify to the parties the date and place of hearing of the appeal, and send a copy of the memorandum of appeal to the respondent either before or with such notice.

21. The date and place of hearing of the appeal shall be fixed with reference to the current business of the Tribunal and the time necessary

for the service of the notice of appeal, so as to allow the parties sufficient time to appear and be heard in support of, or against the appeal.

22. In an appeal under sub-section (1) of Section 33, in fixing the date for the respondent to appear and answer to the appeal, a reasonable time shall be allowed for the necessary communication with the Commissioner through the proper channel and for the issue of instructions to an authorised representative to appear and answer on behalf of the respondent.

23. On the day fixed, or any other day to which the hearing may be adjourned, the appellant shall be heard in support of the appeal. The Tribunal shall then, if it does not dismiss the appeal at once, hear the respondent against the appeal, and in such case the appellant shall be entitled to reply.

24. Where on the day fixed for hearing or any other day to which the hearing may be adjourned, the appellant does not appear when the appeal is called on for hearing, the Tribunal may dismiss the appeal for default.

25. Where on the day fixed for hearing or any other day to which the hearing may be adjourned, the appellant appears and the respondent does not appear when the appeal is called on for hearing, the Tribunal may hear the appeal ex-parte.

Explanation :—In rules 24 and 25 " appear " means appear in person or through an authorised representative.

26. Where an assessee whether he be the appellant or the respondent to an appeal dies or is adjudicated insolvent or in the case of a company is being wound up, the appeal shall not abate and may, if the assessee was the appellant, be continued by, and if he was the respondent be continued against, the executor, administrator or other legal representative of the assessee or by or against the receiver or liquidator as the case may be.

27. The respondent, though he may not have appealed, may support the order of the Appellate Assistant Commissioner on any of the grounds decided against him.

28. Where the Tribunal is of opinion that the case should be remanded, it may remand it to the Appellate Assistant Commissioner or the Income-tax Officer, with such directions as the Tribunal may think fit.

29. The parties to the appeal shall not be entitled to produce additional evidence either oral or documentary before the Tribunal, but if the Tribunal requires any document to be produced or any witness to be examined or any affidavit to be filed to enable it to pass orders or for any other substantial cause, or if the Income-tax Officer has decided the case without giving a sufficient opportunity to the assessee to adduce evidence either on points specified by him or not specified by him, the Tribunal may allow such document to be produced or witness to be examined or affidavit to be filed or may allow such evidence to be adduced.

30. Such document may be produced or such witness examined or such evidence adduced either before the Tribunal or before the Appellate Assistant Commissioner or before the Income-tax Officer as the Tribunal may direct.

31. If the document is directed to be produced or witness examined or evidence adduced before the Appellate Assistant Commissioner or the Income-tax Officer, he shall comply with the direction of the Tribunal and after compliance send the document, the record of the deposition of the witness or the record of the evidence adduced, to the Tribunal.

32. The Tribunal may, on such terms as it thinks fit, and at any stage adjourn the hearing of the appeal.

33. (1) The order of the Bench shall be in writing and shall be signed and dated by the members constituting it.

(2) Where a case is referred under sub-section (7) of Section 5A, the order of the member or members to whom it is referred shall be signed and dated by him or them as the case may be.

34. The Tribunal shall, after the order is signed, cause it to be communicated to the assessee and to the Commissioner.

35. An application for reference under sub-section (1) of Section 66 shall be in triplicate and shall be accompanied by a list of documents (particulars of which shall be stated) which the applicant desires to be forwarded to the High Court, and a translation in English of any such document where necessary.

36. Rules 7, 8, 13, 20, 21, 22, 23, 26 and 33 shall apply, *mutatis mutandis*, to an application under sub-section (1) of Section 66.

37. Where the application is by an assessee, the Commissioner to whom the Income-tax Officer is subordinate, shall be made a respondent.

38. Where the application is by the Commissioner, the assessee shall be made a respondent.

39. The Bench which heard the appeal giving rise to the application shall hear it unless the President directs otherwise.

40. On receipt of the notice of the date of hearing of the application, a respondent shall, at least 7 days before the date of hearing, submit a reply in writing to the application.

41. The reply to the application shall specifically admit or deny whether the question of law formulated by the applicant arises out of the order under sub-section (4) of Section 33. If the question formulated by the applicant is defective, the reply shall state in what particular the question is defective and what is the exact question of law which arises out of the said order. The reply shall be accompanied by two copies thereof, a list of documents (the particulars of which shall be stated) which the respondent desires to be forwarded to the High Court and a translation in English of any such document, where necessary.

42. On the day fixed for the hearing of the application or any other day to which the hearing may have been adjourned, after hearing the parties, the Tribunal shall dismiss the application, if it is of opinion that no question of law arises out of the order passed under sub-section (4) of Section 33.

43. Where the Tribunal is of opinion that a question of law arises out of the order under sub-section (4) of Section 33, it shall draw up a statement of the case.

44. The Tribunal shall append to the statement documents (which shall be listed) which in its opinion, may be required by the High Court at the hearing of the reference.

45. The order on the application for reference shall be communicated to the assessee and the Commissioner.

46. Where a requisition is received from the High Court under sub-section (2) of Section 66, or where the case is referred back under sub-section (4) of the said section, it shall be dealt with by the Bench referred to in rule 39 unless otherwise directed by the President.

47. When a copy of the judgment of the High Court is received by the Tribunal under sub-section (5) of Section 66, it shall be sent to the Bench referred to in rule 39 for such orders as may be necessary unless the President directs otherwise.

48. (1) The scales of copying fees, where chargeable shall be as under :—

(a) For the first 200 words or less—

English.	... As. 12
Vernacular.	... As. 6

(b) For every additional 100 words or fraction thereof—

English.	... As. 6
Vernacular.	... As. 3

A uniform extra fee of Re. 1 shall be charged on an application for urgent copies.

(2) The Tribunal may supply to both parties free of cost and without application one copy of its order under sub-section (4) of Section 33 or of any order passed or statement drawn up by it under Section 66.

49. The scales of inspection fee shall be as under :—

(a) For each hour or part of an hour for ordinary inspection.	... Re. 1. (Court fee stamp).
(b) For each hour or part of an hour for urgent inspection.	... Rs. 2. (Court fee stamp).

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